

UNITED STATES BANKRUPTCY COURT  
DISTRICT OF NEVADA  
LAS VEGAS DIVISION

IN RE: ) CASE NO: 06-10725  
) CHAPTER 11  
)  
USA COMMERCIAL MORTGAGE COMPANY, ) Las Vegas, Nevada  
)  
) Thursday, May 18, 2006  
Debtor. ) ( 9:49 a.m. to 12:22 a.m.)  
) (12:32 p.m. to 1:11 p.m.)

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IN RE: USA CAPITAL REALTY )  
ADVISORS, LLC., ) CASE NO: 06-10726  
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IN RE: USA CAPITAL DIVERSIFIED )  
TRUST DEED FUND, LLC., ) CASE NO: 06-10727  
)

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IN RE: USA CAPITAL FIRST TRUST )  
DEED FUND, LLC., ) CASE NO: 06-10728  
)

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IN RE: USA SECURITIES, LLC., ) CASE NO: 06-10729  
)

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MOTIONS HEARING

BEFORE THE HONORABLE LINDA B. RIEGLE,  
UNITED STATES BANKRUPTCY JUDGE

Calendared Motions: See pages 2, 3

Appearances: See pages 3, 4, 5

Court Recorder: Araceli Catu

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CALENDARED MOTIONS:

06-10725: USA COMMERCIAL MORTGAGE COMPANY

1 MOTION OF THE DEBTORS PURSUANT TO SECTIONS 363(b) AND 105(a) OF THE BANKRUPTCY CODE FOR AUTHORIZATION TO PAY PREPETITION WAGES, COMPENSATION AND EMPLOYEE BENEFITS;

2 APPLICATION TO EMPLOY SCHWARTZER & MCPHERSON LAW FIRM AS COUNSEL UNDER GENERAL RETAINER;

3 MOTION AUTHORIZING DEBTOR, PURSUANT TO 11 U.S.C. 105 AND 363(b)(1), TO ACCEPT LOAN PAYMENT PROCEEDS AND PROVIDE PARTIAL RELEASES OR FULL RELEASES IN CONNECTION WITH THE SALE OF PROPERTIES SECURING LOANS ORIGINATED BY THE DEBTOR TO THIRD-PARTY BORROWERS, AND TO RATIFY PARTIAL RELEASES PREVIOUSLY PROVIDED BY THE DEBTOR;

06-10726: USA CAPITAL REALTY ADVISORS, LLC

1 MOTION OF THE DEBTORS PURSUANT TO SECTIONS 363(b) AND 105(a) OF THE BANKRUPTCY CODE FOR AUTHORIZATION TO PAY PREPETITION WAGES, COMPENSATION AND EMPLOYEE BENEFITS;

2 APPLICATION TO EMPLOY RAY QUINNEY & NEBEKER P.C. AS COUNSEL FOR THE DEBTORS

06-10727: USA CAPITAL DIVERSIFIED TRUST DEED FUND, LLC

1 MOTION OF THE DEBTORS PURSUANT TO SECTIONS 363(b) AND 105(a) OF THE BANKRUPTCY CODE FOR AUTHORIZATION TO PAY PREPETITION WAGES, COMPENSATION AND EMPLOYEE BENEFITS;

2 MOTION TO LIMIT NOTICE AND APPROVE MASTER SERVICE LIST FOR LIMITED NOTICE

06-10728: USA CAPITAL FIRST TRUST DEED FUND, LLC

1 MOTION OF THE DEBTORS PURSUANT TO SECTIONS 363(b) AND 105(a) OF THE BANKRUPTCY CODE FOR AUTHORIZATION TO PAY PREPETITION WAGES, COMPENSATION AND EMPLOYEE BENEFITS;

2 MOTION TO LIMIT NOTICE AND APPROVING MASTER SERVICE LIST FOR LIMITED NOTICE

CALENDARED MOTIONS: (CONTINUED)06-10729: USA SECURITIES, LLC

1 MOTION OF THE DEBTORS PURSUANT TO SECTIONS 363(b) AND 105(a) OF THE BANKRUPTCY CODE FOR AUTHORIZATION TO PAY PREPETITION WAGES, COMPENSATION AND EMPLOYEE BENEFITS;

2 MOTION TO LIMIT NOTICE, MOTION APPROVING MASTER SERVICE LIST FOR LIMITED NOTICE

COURTROOM APPEARANCES FOR:

Debtors: P.O. Box 45385  
Salt Lake City, UT 84145

LENARD SCHWARTZER, ESQ.  
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Official Committee of USA Capital First Trust Deed Fund, LLC, et al.: FRANK MEROLA, ESQ.  
EVE KARASIK, ESQ.  
JEFFREY DAVIDSON, ESQ.  
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Official Committee of Equity Security Holders of USA Capital First Trust Deed Fund, LLC: CANDACE CARLYON, ESQ.  
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Stanley Alexander Trust, et al.: ROBERT LE POME, ESQ.  
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COURTROOM APPEARANCES FOR: (CONTINUED)

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Fortress Credit Corp.:	JOEL SAMUELS, ESQ. SIDLEY AUSTIN, LLP (No address provided)
Canepa Group:	LAUREL DAVIS, ESQ. Fennemore Craig, P.C. 300 S. Fourth Street, #1400 Las Vegas, NV 89101
Dr. Gary Kantor, et al.:	RICHARD J. MASON, ESQ. McGuire Woods 130 Pinetree Lane Riverwoods, IL 60015
Aspen Square Management, Inc., et al.:	ROBERT KINAS, ESQ. Snell & Wilmer, LLP 3883 Howard Hughes Parkway, #1100 Las Vegas, NV 89169
Buckalew Trust, et al.:	GREG GARMAN, ESQ. Morgan Silver 3960 Howard Hughes Parkway 9th Floor Las Vegas, NV 89169
Bank of America:	SCOTT FLEMING, ESQ. Hale Lane, et al. 3930 Howard Hughes Parkway 4th Floor Las Vegas, NV 89169
Margaret McGimsey, et al.:	WILLIAM MCGIMSEY, ESQ. 3017 W. Charleston Blvd., #30 Las Vegas, NV 89102
Harvey Family Trust, date April 13, 1987:	DONNA OSBORN, ESQ. MARK ORBACH, ESQ. Wright, Finlay & Zak, LLP 5532 S. Fort Apache Road Suite 110 Las Vegas, NV 89148
<u>COURTROOM APPEARANCES FOR:</u> (CONTINUED)	

Project Disbursement  
Group:

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U.S. Trustee:

AUGIE LANDIS, ESQ.  
Assistant United States Trustee  
(No address provided)

Shauna M. Walch, et al.: GREGORY J. WALCH, ESQ.  
400 S. Fourth St.  
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Las Vegas, NV 89101

Roam Development Group,  
LP, et al. MARJORIE GUYMON, ESQ.  
Goldsmith & Guymon, P.C.  
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Las Vegas, NV 89134

TELEPHONIC APPEARANCE FOR:

Group of Direct Lenders: JANET CHUBB, ESQ.  
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12th Floor.  
P.O. Box 281  
Reno, NV 89504

Las Vegas, Nevada; Thursday, May 18, 2006; 9:49 a.m.

(Call to Order)

**THE COURT:** Okay. *USA Commercial Mortgage Company* and related companies. Appearances by attorneys, please.

**THE CLERK:** And we have one the phone.

**MS. JARVIS:** Annette Jarvis and Lenard Schwartz on behalf of the debtors.

**MR. MEROLA:** Good morning, your Honor; Frank Merola, Eve Karasik, Jeffrey Davidson, members of Stutman Treister and Glatt, Professional Corporation, on behalf of the official committee of USA Capital First Trust Deed Fund, LLC, the unofficial committee of USA Capital Diversified Trust Fund, LLC, and the official committee of executory contract holders of USA Commercial Mortgage Company, the investor committees from here on in.

**MS. CARLYON:** Good morning, your Honor, Candace Carlyon of Shea and Carlyon, proposed special Nevada counsel for the investor committees.

**MR. LE POME:** Robert LePome for Dr. Stanley and twenty other direct lenders.

**MR. CONNAGHAN:** Paul Connaghan with Susan Scann of Deaner Deaner Scann Malan and Larsen, on behalf of the seven borrower entities I listed on the sign-in sheet.

Do you need me to name those?

**THE COURT:** Yes.

1           **MR. CONNAGHAN:** Interstate Commerce Center, LLC, ISCC  
2 Phase Two, LLC, Copper Sage Commerce Center, LLC, I-40 and  
3 Gateway West, LLC, Rio Rancho Executive Plaza, LLC, Franklin  
4 Stratford Investments, LLC, Boise Gala Ninety-Three, LLC.

5           **THE COURT:** Okay. And these are borrowers?

6           **MR. CONNAGHAN:** Yes, your Honor.

7           **THE COURT:** Okay, thank you.

8           **MR. CONNAGHAN:** Thank you.

9           **THE COURT RECORDER:** Excuse me, sir; can you spell  
10 your name for me? Thank you.

11           **MR. CONNAGHAN:** C-o -- Paul -- C-o-n-n-a-g-h-a-n.

12           **THE COURT RECORDER:** Thank you.

13           **MR. SAMUELS:** Good morning, your Honor; Joel Samuels  
14 of Sidley Austin, LLP, for Fortress Credit Corporation.

15           **MS. DAVIS:** Good morning, your Honor; Laurel Davis on  
16 behalf of the Canepa Group.

17           **MR. MASON:** Good morning, Judge Riegle. For the  
18 record, my name is Richard J. Mason. I'm with a law firm  
19 called McGuire Woods, and we represent Dr. Gary Kantor and  
20 certain related employee benefit plans which in the aggregate  
21 are one of the large --

22           **(A cell phone rings)**

23           **THE COURT:** All cell phones must be off. Take time  
24 now and turn them off.

25           Sorry.

1           **MR. MASON:** As I was saying, one of the larger  
2 investors in the USA Commercial group.

3           **MR. KINAS:** Good morning, your Honor; Robert Kinas of  
4 Snell and Wilmer, for a variety of the direct lenders.

5           **MR. GARMAN:** Greg Garman with Morgan Silver on behalf  
6 of Higgins and Buckalew Trust which are both direct lenders.

7           **MR. FLEMING:** Good morning, your Honor; Scott Fleming  
8 of Hale Lane on behalf of Bank of America.

9           **MR. MCGIMSEY:** William McGimsey on behalf of Margaret  
10 McGimsey and others, investors in the Diversified Trust Deed  
11 Fund.

12           **MS. OSBORN:** Donna Osborn and Mark Orbach (phonetic)  
13 on behalf of Rodrick Harvey and Pauline Harvey, trustee of the  
14 Harvey Family Trust, direct lenders.

15           **MR. CALLISTER:** Good morning, your Honor; Matthew  
16 Callister on behalf of Project Disbursement Group.

17           **MR. LANDIS:** Good morning, your Honor; Augie Landis,  
18 Assistant United States Trustee.

19           **MR. WALCH:** Good morning, your Honor; Gregory Walch  
20 on behalf of the Gregory J. and Shauna M. Walch Family Trust.

21           **MS. GUYMON:** Good morning, your Honor; Marjorie  
22 Guymon appearing on behalf of Roam Development Group, LP,  
23 borrower. Also appearing on behalf of Mountain West Mortgage  
24 in relation to Larren Hills (phonetic) Project and the Marlton  
25 (phonetic) Square Project, direct lenders, and individual



1 Michael Gortz.

2 **THE COURT:** Okay. And on the telephone?

3 **MS. CHUBB:** Janet Chubb of Jones Vargas for a group  
4 of direct lenders.

5 **THE COURT:** And Ms. Chubb called back in, right?  
6 This is not --

7 **THE CLERK:** Yes.

8 **THE COURT:** Okay. And just to make -- I know you're  
9 aware, your participation is just to monitor only. I'm not  
10 going to allow any representations or comments.

11 **MS. CHUBB:** I understand.

12 **THE COURT:** We were hoping to have a phone system in,  
13 but due to some errors on my part trying to arrange the  
14 contracts, we don't have that yet. But in any case, just for  
15 clarification, I think this case is going to be impossible to  
16 have any -- to allow phone participation where there are  
17 objections that one argues. It's just too hard to do. But in  
18 light of the need for people to monitor, I don't have a problem  
19 with you monitoring.

20 Okay, just a few comments before we start. First,  
21 just to remind all those people who are not attorneys who may  
22 be investors or who may be members in the various companies,  
23 this is not the same thing as a 341 meeting. This is not the  
24 time that you raise objections or ask questions. I'm here to  
25 hear and determine the issues that are brought before me by

1 pleadings and motions, and those are the only issues that we're  
2 hearing and deciding today, so, please understand that.

3 Now, just some procedural matters. I am serious  
4 about late oppositions and courtesy copies. For example, I  
5 received one opposition yesterday, and I was told the attorney  
6 was going to bring me the courtesy copy this morning.

7 Now, I don't know how anybody expects this case to  
8 progress, if you want me to be well-informed and want me to  
9 review it, if you think you can file your opposition at the  
10 last minute and not give us any copies. And this motion was  
11 properly served, so this opposition was late by any standards.

12 So I've entered an order in this case and it's  
13 already out there, that says that any opposition must be filed  
14 the earlier of fifteen days after service or five days before  
15 the hearing. I am going to enforce that. From now on, any  
16 late opposition is subject to being stricken and three hundred  
17 dollars payable to the movant. If you don't provide a reply  
18 copy within twenty-four -- sorry, a courtesy copy within  
19 twenty-four hours after the filing, I will impose a sanction of  
20 seventy-five dollars payable to the Court.

21 Now, this may seem harsh, but as you can see, there  
22 are hundreds of pleadings in this case, and the only way that I  
23 can be informed, the only way that people can respond to  
24 objections meaningfully and intelligently is to have it on a  
25 timely basis. And unfortunately, Mr. Kinas wasn't in the room

1 when I explained all this.

2 Mr. Kinas, no more late oppositions.

3 **MR. KINAS:** I understand, your Honor. We are  
4 contacted almost hourly by many direct lenders with sensitive  
5 issues. To the extent that they would like to bring those to  
6 your attention, we will certainly request permission to file  
7 those. But we were very sensitive to the Court's earlier order  
8 on scheduling.

9 **THE COURT:** Okay.

10 All right, so let's go to the first motion we have.  
11 The first motion that was already dealt with; that shouldn't  
12 have been on calendar. The motion to pay wages, that's  
13 correct, there was nothing left in that regard?

14 **MR. SCHWARTZER:** Yes, your Honor. You've already  
15 entered an order on that on April 17th.

16 **THE COURT:** All right. So next we have --

17 **THE COURT RECORDER:** Stay closer to the microphone.  
18 Thank you.

19 **MR. SCHWARTZER:** I will.

20 **THE COURT:** Oh, and just for clarification. Because  
21 our transcription works only by virtue of the microphone, what  
22 happens is the person here is only taking notes. All we have  
23 is a tape recording. If anybody wants a transcript, you need  
24 to order a transcript from the Court transcriber or the Court  
25 personnel, and they will then order a transcript from the

1 company that provides transcripts.

2 Alternatively, you can receive a tape or a CD of the  
3 proceedings for a cost. So we don't have a system whereby  
4 somebody is automatically going to come out with notes.  
5 Therefore, it's vitally important that, because someone sitting  
6 in Nampa, Idaho, is transcribing this, that's why it's  
7 important that you always speak into the microphone and speak  
8 very clearly.

9 For that reason, either be at the podium speaking  
10 into the microphone. If you're at the desk, I very appreciate  
11 the protocol in standing and rising before the Court, but I  
12 will excuse that because, unfortunately, the protocol must --  
13 good transcripts have to trump protocol, so I will understand  
14 if you remain seated while you're at the desk.

15 Probably the best thing is if you're just speaking  
16 yourself is to come to the podium, but if you're just making a  
17 comment, I'll allow you to remain seated.

18 Okay, the first thing we have is the application to  
19 employ the attorneys.

20 **MS. JARVIS:** If I may, your Honor, I'd like to make  
21 the legal arguments both on behalf of Ray Quinney and  
22 Schwartzter and McPherson and then have Mr. Schwartzter add to  
23 that afterwards, because it involves the same issues.

24 **THE COURT:** Right.

25 **MS. JARVIS:** These applications have been noticed to

1 all investors and creditors. They went out to the entire  
2 mailing matrix. Only two objections were filed plus one  
3 limited objection that I believe we have resolved.

4           The major objection in this case was filed by the  
5 U.S. trustee, and the U.S. trustee claims that Ray Quinney and  
6 Nebeker and Schwartz and McPherson are disqualified to  
7 represent all the debtors because they claim there is an actual  
8 conflict of interest that exists between the various estates,  
9 or, if not actual, a potential conflict of interest that  
10 prohibits the retention of the two law firms by all of the  
11 debtors.

12           There are no actual conflicts of interest between  
13 these estates, and to the extent there may be potential  
14 conflicts of interest, these do not prohibit our retention  
15 under the law.

16           The trustee cites the definition of actual conflict  
17 of interest from the *Mercury* case, which is a case from the  
18 Southern District of New York, as, quote, 'an actual competing  
19 -- an active, competing title between two interests in which  
20 one interest can be served only at the expense of the other.'

21           The *Roberts* case which is also cited in the *Mercury*  
22 case, the *Roberts* case from Utah, which is actually a very oft-  
23 cited case, provides perhaps even a more complete statement of  
24 what the test is with respect to adverse interest. In that  
25 case, the Court explained an adverse interest is where two or

1 more entities, quote, 'possess or assert mutually exclusive  
2 claims to the same economic interest', close quote, which  
3 creates a dispute between rival claimants as to which of them,  
4 quote, 'the disputed right or title to the interest in question  
5 attaches under applicable law.' So in other words, there is a  
6 situation where only one or the other can win with respect to  
7 the same economic interest or the same property.

8           The U.S. trustee raises two situations that it claims  
9 create an actual conflict of interest. The first is that there  
10 are amounts purportedly due from the funds to Commercial  
11 Mortgage for overpayments due to non-performing loans; and the  
12 second is the loan servicing fees issue.

13           As to the first issue, even the U.S. trustee admits  
14 that this is purportedly owed and acknowledges at this point in  
15 time this is really only a potential conflict of interest  
16 because it is not yet determined whether anything is owed, and  
17 that is part of the ongoing investigation of Mr. Alison that  
18 has been allowed for ninety days.

19           And I think as your Honor hopefully read in our reply  
20 brief, we are limiting at this point our application to be  
21 hired consistent with what the Court has already allowed  
22 Mr. Alison to be retained. So for the ninety days, pending the  
23 further report of the Court and the further looking at the  
24 issues to see in fact if in that case whether there are any  
25 unexpected conflicts that -- potential or actual conflicts that

1 might arise to be dealt with at that point in time.

2           Now, there is one fact or one piece of progress that  
3 has been made in this case that was reported yesterday at the  
4 341 meeting that actually is relevant to this situation.  
5 Mr. Alison has already collected -- I think your Honor knows  
6 that previously we've reported that there was \$50 million  
7 dollars of past-due interest that had not been collected and  
8 that had been paid out. Mr. Alison has been working hard at  
9 collecting that interest, and to date has either commencements  
10 or collected \$12 million dollars of that outstanding amount,  
11 and therefore that would be almost twenty-five percent of the  
12 past-due interest.

13           Now, this is relevant because of course if he is  
14 successful in collecting all this past-due interest, then this  
15 issue of overpayment is completely resolved, because the money  
16 would have come in and there is no remaining issue with respect  
17 to that.

18           But even if some amount is determined to be owing, it  
19 is really an accounting determination; it's not one that's  
20 going to be subject to dispute, and that is not -- would not  
21 fit within the definition of adverse interest as set forth in  
22 the *Roberts* case. So at most this raises a potential conflict  
23 of interest, but that does not even look likely that it's going  
24 to ripen into an actual conflict of interest.

25           The fact I think that the fund committee counsel that

1 did file limited opposition does not raise this issue  
2 reinforces the position that the debtor is taking, that these  
3 are not actual conflicts of interest.

4           With respect to the loan servicing fee, that exists  
5 between the funds and USA Mortgage. There is no evidence  
6 before the Court that there is a dispute with respect to that  
7 fee. Both Commercial Mortgage and the funds have a common  
8 interest, and that common interest is to collect on all the  
9 non-performing loans and to make sure that the loans that are  
10 performing continue to pay for the benefit of those funds and  
11 other investors.

12           And those collection actions are facilitated and  
13 allowed by the existence of the loan servicing agreement which  
14 allows Commercial Mortgage to act on behalf of the hundreds of  
15 investors that are in each loan.

16           It's mere speculation that is raised that there is  
17 some conflict or that there would be a dispute or conflict that  
18 is raised by the U.S. trustee's office, and mere speculation is  
19 not sufficient to disqualify Ray Quinney and Nebeker and  
20 Schwartzer and McPherson from representing the debtors. Nor is  
21 this a type of lucrative contract which was referred to in the  
22 *Interwest Business* case (phonetic) that is cited in the U.S.  
23 trustee's objection. These are sophisticated investors that  
24 agreed to loan servicing fee, and no one has raised the issue  
25 that these fees are anything unusual in the industry or



1 unreasonable.

2           The budget approved by the Court two weeks ago I  
3 think kind of evidences that because, of course, the budget,  
4 which is based solely on the servicing fees for the many  
5 services that need to be performed in order to collect on these  
6 loans is very slim with respect to the many things that the  
7 servicer needs to do for the funds.

8           I would like further to note that the *Interwest* case,  
9 which is out of the Tenth Circuit and therefore is a case I'm  
10 very familiar with, that it involved a view on whether there  
11 can be representations of affiliate debtors. And that case has  
12 not been followed by any other circuit. And in fact, in the  
13 Tenth Circuit itself, it has been quite liberally interpreted,  
14 as it needs to be, even though the fact that it exists out  
15 there, frankly is a problem for us in the Tenth Circuit with  
16 respect to having any complex cases filed in our circuit.

17           But it does not even say that absolutely even in the  
18 most -- because it is the most extreme case, that you can't  
19 have one counsel representing affiliate debtors. It simply  
20 says that you have to look at this on a case by case basis. It  
21 does not say that it is per se prohibited. So even that most  
22 extreme case would not support not allowing Ray Quinney and  
23 Nebeker and Schwartz and McPherson to represent all these  
24 debtors.

25           Nor does the *Wheatfield* (phonetic) case, which is

1 also cited by the U.S. trustee in their objection, because it  
2 deals with actual conflicts of interest which are not present  
3 in this case. And it recognizes that potential conflicts of  
4 interest come in enormously varying degrees, and that those  
5 have to be looked at on a case by case basis, and it's only if  
6 a potential conflict is sufficiently important and there is  
7 more than a sufficient likelihood that it will ripen into an  
8 actual conflict that potential conflicts become a problem with  
9 respect to retention of counsel for more than one debtor. And  
10 that has not been shown to be the case here.

11           The third case cited by the U.S. trustee in their  
12 response which is also out of the Central District of  
13 California, that case as well actually does not -- besides in a  
14 footnote, it simply addresses the issue of whether in a  
15 substantive consolidation situation, it would have been better  
16 to have a single counsel or several counsel, and the Court  
17 simply expresses an opinion about that, but it wasn't confirmed  
18 by the Ninth Circuit because it's in footnote, it's dicta, so  
19 that was not, you know, accepted, and it's also factually  
20 distinguishable from our case here.

21           The application of Ray Quinney and Nebeker and  
22 Schwartz and McPherson is consistent with the results in many  
23 cases that have been cited in our reply brief. The *OPM Leasing*  
24 case, the *Wheatfield Village* case, the *International Oil* case,  
25 the *Global Marine* case, all of these recognize when you have

1 any kind of debtor where you have several affiliates, which is  
2 often the way debtors are organized and they have common cash  
3 management systems, that these kind of ordinary course,  
4 undisputed, inter-company debts that they do not prohibit the  
5 joint representation of those debtors by a single counsel.

6 And again, we've asked for this to be limited to  
7 ninety days while Mr. Alison does continue his investigation.  
8 We'll file a report to the Court, and at that point in time, if  
9 something unexpected comes up, something that we don't know at  
10 present, that obviously will be revisited both with respect to  
11 Mr. Alison and with us.

12 And of course Mr. Alison now is trying to go through  
13 this, and for him to have to report to more than one counsel, I  
14 don't know that he could even figure out which counsel he'd  
15 have to report to because the issues at present are common and  
16 there are no actual conflicts of interest.

17 Let me finally just address the issue with potential  
18 conflicts of interest, because there is one more issue that was  
19 raised. Again, there is not a case which says potential  
20 conflicts of interest are absolutely disqualifying nor inter-  
21 company debt. And in fact when you look at Section 327(c),  
22 because it says that, you know, a counsel can represent a  
23 creditor and also represent the debtor unless there is an  
24 objection and the Court determines an actual conflict, that in  
25 and of itself I think clearly says that the mere existence of

1 an inter-company debt does not disqualify counsel unless there  
2 is an actual conflict of interest, which there is not in this  
3 case.

4           The only other potential conflict of interest that  
5 was raised by the U.S. trustee is that in Mr. Alison's  
6 declaration it says there is a \$58 million dollar inter-company  
7 receivable which is owed by a non-debtor entity, USA Investment  
8 Partners, to USA Commercial Mortgage, and in his declaration he  
9 says 'and possibly to other debtors'.

10           As Mr. Alison testified yesterday in the 341 meeting,  
11 he is currently unaware of any other debtors having debts owed  
12 to them by IP other than Commercial Mortgage. However, that is  
13 obviously subject to careful tracing of disbursements from all  
14 the debtors, and if those amounts, if there are other debts  
15 owed by this non-debtor entity, those obviously will be  
16 documented and pursued. But if that happens, it's not an issue  
17 where you are fighting about who has which debt or who has this  
18 \$58 million dollar debt. That is established. It is whether  
19 there are additional debts that may be owed that are separate  
20 and distinct from that, and that does not create a potential  
21 conflict of interest.

22           In fact, with respect to the negotiations that  
23 Mr. Alison has been having with Investment Partners to secure  
24 the \$58 million dollar debt in recognition that as these  
25 investigations continue, there may be more debts discovered,

1 the documents that he has negotiated do recognize in the UCC  
2 filing the possibility that it would be filed in essence on  
3 behalf of all the debtors just in case there is something else  
4 that would arise from another debtor in order to protect all of  
5 their interests.

6 So here I think where we have no actual conflicts of  
7 interest that have been demonstrated, and that if there are  
8 potential conflicts of interest, they are, as said in the *OPM*  
9 case, decidedly more apparent than real. This does not provide  
10 a basis for not allowing the retention by all of the debtors  
11 for Ray Quinney and Nebeker and Schwartz and McPherson for  
12 the ninety-day period pending a further report to the Court by  
13 Mr. Alison.

14 Let me also state that the debtor has contacted  
15 Mr. Houston, who is here in this court, and if it looks like  
16 that would be a solution, he is willing to serve, and we may  
17 actually just go ahead and file an application to have him  
18 serve as conflicts counsel, in order to deal with any problems  
19 that might arise in the future in the event that, you know,  
20 just as a way of anticipating things rather than waiting to see  
21 if anything unexpected arises.

22 I think this deals with the objection of Mr. McGimsey  
23 as well.

24 Let me finally just say that the first Trust Deed  
25 Fund committee counsel did file an objection, and let me just

1 clarify on that. We are not seeking -- Ray Quinney and Nebeker  
2 is not seeking nor is Schwartzer and McPherson seeking an order  
3 under 328 which establishes our rates as reasonable and not  
4 subject to court review. That is not intended. They clearly  
5 are subject to court review. I understand that in the Ninth  
6 Circuit, you need to be careful with respect to that. And  
7 whether that means that we are not retained under 328 or there  
8 is a clear expression that we are retained but this does not  
9 mean that our rates are not subject to court review as  
10 reasonable. However it needs to be done, we are -- that was  
11 clearly our intention.

12 **THE COURT:** Okay.

13 **MS. JARVIS:** And I think that resolves that.

14 **THE COURT:** I just had a question. This was not  
15 raised with the U.S. trustee, but I think it's probably  
16 appropriate that I raise it. You indicate that you received a  
17 payment -- that you billed some pre-petition and received a  
18 payment on account of that through the retainer.

19 You were not the counsel for the debtor up until  
20 Mr. Mesereaux (phonetic) was involved, correct?

21 **MS. JARVIS:** We became counsel for the debtor merely  
22 in looking towards filing for the bankruptcy, so this --

23 **THE COURT:** Okay. So this is all in connection with  
24 the bankruptcy --

25 **MS. JARVIS:** Yes.

1           **THE COURT:** -- as opposed to past-due services?

2           **MS. JARVIS:** Exactly. And we have agreed that in our  
3 first fee application we will go ahead and disclose all of  
4 that, you know, and account for it so that if anyone has any  
5 objections, that can be raised at that time.

6           **THE COURT:** Okay. I just want to clear that so we  
7 don't have a preference problem, because it was clearly in the  
8 context of the bankruptcy.

9           **MS. JARVIS:** Yes, it was.

10          **THE COURT:** Okay.

11          **MS. JARVIS:** There was nothing done other than  
12 preparing for the bankruptcy.

13          **THE COURT:** Okay. All right, I don't think you need  
14 to do anything, unless you want to, Mr. Schwartz; opposition  
15 or comments?

16               Before you start, Mr. Landis, and I was remiss in  
17 probably not doing a little status before we started, but some  
18 of this is more appropriate for you. Tell me what happened at  
19 the 341 meeting vis-à-vis committees so that I understand  
20 exactly where we are on committees and who represents who.

21          **MR. LANDIS:** Thank you, Judge. And actually,  
22 yesterday was a very busy day in connection with all of these  
23 matters.

24               With respect to committees, there were four that have  
25 been formed. There is an unsecured creditors committee for

1 sort of the mother-ship, USA Commercial Mortgage Company.  
2 There is an executory contract holder group through USA  
3 Commercial Mortgage Company, and those would be people I think  
4 in your prior hearing that you referred to as direct lenders.

5 **THE COURT:** Okay. So these are the direct lenders?

6 **MR. LANDIS:** Yes. And the reason that they're  
7 identified as executory contract holders is their rights as  
8 direct lenders accrue through their loan servicing agreements  
9 with USA Commercial Mortgage, their rights and their  
10 obligations. That's the reason why they've been characterized  
11 in the fashion that they have. We think it's appropriate under  
12 the Code to appoint a group to represent those folks because  
13 they are a significant component of the overall investor  
14 universe that you're dealing with here.

15 **THE COURT:** I may quarrel with the title; I don't  
16 quarrel for the need for such a committee.

17 **MR. LANDIS:** Fair enough.

18 With respect to the two fund committees, one equity  
19 security holder committee for each fund. And that is the sum  
20 and substance of the committees that have been appointed in  
21 these cases.

22 The two remaining entities, it was clear from the  
23 341, don't continue to operate, have no employees and no  
24 substantive debt that would need to be represented by a  
25 committee, and that's the reason why there weren't committees



1 appointed in those cases.

2           The organizational meeting of all of the committees  
3 I've just identified for you occurred yesterday morning prior  
4 to the 341 meets. I can tell you that there have been -- well,  
5 there was essentially a beauty contest if you will for all the  
6 attorneys, various financial folks, probably some accountants.  
7 There was a number of people who wanted to meet with the  
8 committees yesterday. The committees did a great job of being  
9 organized and allowing people to come in after their committee  
10 work was established.

11           Had there been a longer period of time, I think they  
12 would have gotten to see everyone. I think they got to see  
13 plenty of folks, and they are well under way in terms of their  
14 operations.

15           I think you've heard appearances now, at least from  
16 one set of counsel, who have appeared on behalf of --

17           **THE COURT:** At least think they won the beauty  
18 contest.

19           **MR. LANDIS:** Well, the application is not here but I  
20 expect it will be coming in the near term.

21           **MR. MEROLA:** It was filed this morning, your Honor.

22           **THE COURT:** Okay.

23           **MR. LANDIS:** Well, there you have it. So I'm sure  
24 we'll visit about that, I believe, probably on shortened time  
25 at the end of June hearing that's coming up next.

1 But bottom line, Judge, is we think that the  
2 committees are well-organized, they're motivated, they have  
3 looked at, seriously, retention of counsel and other  
4 professionals. I think they're going to do an excellent job in  
5 connection with this case, and I think it's important that they  
6 do.

7 **THE COURT:** Okay.

8 All right, so, go ahead with the opposition. I just  
9 needed that kind of background.

10 **MR. LANDIS:** Thanks, Judge. And we did file this  
11 opposition in connection with the applications by Ray Quinney  
12 and Nebeker and also Schwartz and McPherson.

13 I want to make it very clear for the Court there's  
14 one thing that's not on the table here. The United States  
15 trustee's office is not challenging the credentials of these  
16 firms to represent the debtors in these cases. That's not on  
17 the table and it's not something that's a substance of our  
18 opposition.

19 With respect to the pre-petition payments, I would  
20 say that at paragraph twelve in the Ray Quinney matter, we did  
21 point out the fact of the payment, but because we don't have  
22 schedules or any additional information, it was very hard for  
23 us to raise the issue that you have. We'll address that in the  
24 context of a fee application at a later time.

25 What is on the table before the Court right now

1    though is not the caliber of the attorneys, but whether they  
2    can bring those substantial skills that they have to bear for  
3    each of the clients that they would like to represent. And any  
4    time an attorney undertakes to represent multiple parties, the  
5    risk of conflicts of interest is attendant to that effort, and  
6    that's the essence of our objection.

7           I think you've had a good overview of the nature of  
8    our objection. I want to be specific because really there are  
9    two items that you need to focus on in resolving this  
10   opposition. The first is whether or not there is an actual  
11   conflict of interest based upon the representation of the  
12   multiple debtors by the proposed counsel. If you resolve that  
13   issue and determine that there is an actual conflict of  
14   interest right now, then 327 says that that cannot be  
15   countenanced, and, as a result, it can't be permitted in the  
16   context of the multiple representations that are sought.

17           If, however, you find that there is not an actual  
18   conflict of interest, the question becomes whether there is a  
19   potential conflict of interest that would warrant denial of the  
20   application. What we've pointed out here is that it is  
21   presumptively invalid to represent multiple bankruptcy estates  
22   where one debtor entity is owed debts by others.

23           **THE COURT:** But we do cases that are jointly  
24   administered with inter-company receivables all the time.

25           **MR. LANDIS:** And that very well may be the case.

1           **THE COURT:** With one counsel.

2           **MR. LANDIS:** And that very well may be the case, your  
3 Honor, but that's not -- it's not just the potential for the  
4 fees that we're talking about, and I'll get more into detail  
5 about that as we move forward.

6           Ultimately the question as to whether or not that  
7 potential conflict will ripen sufficiently to warrant  
8 disqualification is in the Court's discretion, but we pointed  
9 out in our papers that any time that there is a question as to  
10 whether or not a conflict exists, that question has to be  
11 resolved in favor of disqualification.

12           I'll walk through the analysis that I've just laid  
13 out for you as best I can. I think we've done a good job in  
14 the papers, Judge, and I know there are a lot of other motions  
15 pending, so I'll try to be brief.

16           First, with respect to the existence of debt between  
17 the entities. You've heard the testimony, or you've heard the  
18 arguments I should say, of counsel with respect to the  
19 potential pre-petition debts that give rise to the actual  
20 conflict we've pointed out. I didn't hear anybody say that  
21 there aren't loan servicing agreements between the two fund  
22 debtors and USA Commercial Mortgage. Those exist.

23           **THE COURT:** But if they're not disputed, if everybody  
24 agrees that, yes indeed, the fund has a servicing agreement and  
25 the fund is owed monies through the conduit of the servicing

1 agreement, then what's the dispute?

2           **MR. LANDIS:** It's the other way. The funds owe money  
3 to USA Commercial Mortgage through the servicing agreement.  
4 And --

5           **THE COURT:** Well, but those are -- Nobody disputes  
6 that, right?

7           **MR. LANDIS:** There isn't any dispute, and that's  
8 exactly what my point is, your Honor, is that the fact of the  
9 existence of the loan servicing agreement isn't even an issue.  
10 They do exist, and as --

11           **THE COURT:** But what is the dispute?

12           **MR. LANDIS:** The dispute is whether or not the  
13 obligations of the funds to make payments to USA Commercial  
14 Mortgage generate an actual conflict of interest.

15           You have five estates before you. This is not a  
16 substantively consolidated case.

17           **THE COURT:** No, I understand that.

18           **MR. LANDIS:** So you have three funds or three  
19 different estates at issue with respect to loan servicing. You  
20 have the first Trust Deed Fund, Diversified Fund, and they're  
21 having servicing through USA Commercial Mortgage. They pay USA  
22 Commercial Mortgage for those loan servicings.

23           And yesterday at the 341 hearing, to supplement my  
24 earlier comments, it's about \$200,000.00 through one fund and  
25 about a hundred thousand, a hundred and seven I believe the

1 testimony was, monthly that goes out of the funds and to USA  
2 Commercial Mortgage in connection with those loan servicing  
3 obligations.

4 **THE COURT:** Well, it's really the opposite isn't it?  
5 In other words, the money comes in, it's deducted from the top  
6 and then it goes back?

7 **MR. LANDIS:** Actually --

8 **THE COURT:** No money goes directly from the fund to  
9 USA Commercial; it goes the other way. The money comes in from  
10 the borrower, the servicing fees are taken from the top, and  
11 the rest goes to the fund, correct?

12 **MR. LANDIS:** And to the extent that that's right,  
13 then the question is: How else does USA Commercial Mortgage get  
14 paid by the funds? And the testimony was \$300,000.00 a month  
15 comes from the funds back to USA Commercial Mortgage.  
16 Regardless of which direction it flows, the obligation is  
17 owed --

18 **THE COURT:** Well, how is that any different from  
19 being serviced by somebody else?

20 **MR. LANDIS:** You're right; it's not, and that's the  
21 next thing, your Honor. It's in USA Commercial Mortgage's best  
22 interest to make absolutely certain that the funds do nothing  
23 to eliminate those servicing agreements because that's how they  
24 get paid. And USA Commercial Mortgage, pursuant to the loan  
25 servicing agreements, expects to receive money as a result of

1 those servicing contracts.

2 The bottom line is, is that if an attorney for USA  
3 Commercial Mortgage says to the funds, 'You've got to keep  
4 going', and the funds believe that they're giving him  
5 independent advice --

6 **THE COURT:** Well, the funds can't stop. The point is  
7 the funds have what they have; they're not collecting any more  
8 money. And the point is the funds are lenders of money to  
9 various borrowers either as a percentage interest in some other  
10 loan or, in a few cases, a hundred percent.

11 **MR. LANDIS:** True.

12 **THE COURT:** Okay. So if there's no monies coming  
13 from the fund, there's nothing to stop.

14 **MR. LANDIS:** Your Honor, the point really is: Is  
15 there in fact a debt owed by the funds to USA Commercial  
16 Mortgage pursuant to the loan servicing agreement? And the  
17 answer, I believe, is yeah, there are obligations between the  
18 funds and USA Commercial Mortgage that --

19 **THE COURT:** And why in the world do we want to add  
20 one more layer of expense when we now have a committee? Why in  
21 the world? I mean I understand what you're saying; you're  
22 talking about whether or not there's actual. But let's get to  
23 the practical. Why do you want to make this case DOA by adding  
24 one more layer of expense?

25 **MR. LANDIS:** I don't know necessarily that it becomes

1 DOA by adding --

2 **THE COURT:** Why wouldn't it be?

3 **MR. LANDIS:** Well why would --

4 **THE COURT:** How could it possibly afford one more  
5 layer of expense?

6 **MR. LANDIS:** In terms of having separate counsel for  
7 each of the entities?

8 **THE COURT:** Right.

9 **MR. LANDIS:** The answer is because ultimately then,  
10 each of the entities has independent advice as to what's in  
11 their best interest in all these cases. They can communicate  
12 amongst themselves.

13 **THE COURT:** Why can't that be done through -- Since  
14 the only -- there are no creditors of the funds for the most  
15 part, right, in the usual trade creditor sense? They're all  
16 investors, right?

17 **MR. LANDIS:** Right.

18 **THE COURT:** So why -- And it's unusual, but why is  
19 it, assuming Mr. Merola is counsel, why isn't that need  
20 satisfied by Mr. Merola?

21 **MR. LANDIS:** The answer to your question is when  
22 we're examining the representation of the debtors, we're  
23 looking at the statutory obligations between the debtors and  
24 their counsel. That's what we're examining. The fact that the  
25 committees have representation and can give them independent



1 advice, assuming that they do get that, and we'll cross that  
2 bridge I suspect at a later date.

3 **THE COURT:** Well wouldn't we in essence be having two  
4 counsel representing the same interest if you -- again, in a  
5 case in which you have no trade creditors?

6 **MR. LANDIS:** Well, USA Commercial Mortgage of course  
7 does have that.

8 **THE COURT:** I know; we're talking about the funds.

9 **MR. LANDIS:** Right.

10 **THE COURT:** Because that's where you claim the  
11 conflict is. In a case in which you have no trade creditors,  
12 then why do you want two counsel, one for the debtor and one  
13 for the equity holders, the investors?

14 **MR. LANDIS:** They are always going to have one  
15 counsel for the debtor. The question is who is it going to be,  
16 right?

17 **THE COURT:** Well, but --

18 **MR. LANDIS:** I mean isn't that the essence of it,  
19 Judge? The question is: Who is going to be counsel for the  
20 debtors? Because whether it be Ray Quinney and Nebeker or  
21 someone else, in each of these cases there's still going to be  
22 an attorney for the debtor and there's still going to be an  
23 attorney for the unsecured creditors committee.

24 **THE COURT:** But why wouldn't it be duplication? I  
25 mean again, counsel for the fund, as a debtor counsel, owes his

1 duties to the estate. Well, as it turns out, the estate's  
2 interest, the only people are the investors.

3 Now, I guess, you know arguably I guess you could say  
4 we don't have a debtor's counsel, but that doesn't make sense.

5 **MR. LANDIS:** I agree.

6 **THE COURT:** But why would Mr. Merola's presence  
7 obviate, if there's a conflict, he can recognize it and/or he's  
8 going to articulate those interests?

9 **MR. LANDIS:** Well, A, he hasn't yet been retained, so  
10 we're assuming that --

11 **THE COURT:** Well, someone will be. You have  
12 appointed a committee; someone will be retained.

13 **MR. LANDIS:** Fair enough.

14 **THE COURT:** Okay.

15 **MR. LANDIS:** And equally true is the fact that there  
16 is debtor's counsel, and they're seeking to be retained too.  
17 And we can't ignore the fact that there always will be debtor's  
18 counsel. The question in this matter on this opposition is who  
19 the debtor's counsel is going to be.

20 **THE COURT:** So what do you claim the actual conflict  
21 is today?

22 **MR. LANDIS:** I have laid it out in paragraph twenty  
23 of our opposition, your Honor.

24 **THE COURT:** Okay.

25 **MR. LANDIS:** The loan servicing fees that run between

1 the debtor entities in this case and also --

2 **THE COURT:** But they're undisputed.

3 **MR. LANDIS:** But the fact of the matter is that those  
4 loan servicing arrangements establish obligations between the  
5 parties.

6 **THE COURT:** Okay. Let's go back. Let's assume we  
7 have two affiliated debtors. Parent company makes widgets; the  
8 subsidiary company sells the widgets. Okay, executory contract  
9 between the parties in no way suggests the terms of the  
10 contract are out of the ordinary course of business, there's  
11 money due and owing. Are you saying you couldn't have one  
12 counsel for both cases where there's not a dispute as to the  
13 contract?

14 **MR. LANDIS:** I have cited for the Court the *Interwest*  
15 *Business Equipment* case.

16 **THE COURT:** So you're saying that you could never  
17 have -- under that theory you could never have one debtor --  
18 one attorney for jointly administered debtors under any  
19 circumstance as long as there's any contractual relationship  
20 between the parties?

21 **MR. LANDIS:** What I'm saying, your Honor, is this:  
22 We're only in the first phase of the conflicts analysis under  
23 Section 327(a), and 327(a) says with respect to this retention  
24 that is proposed:

25 'In a case under Chapter 11 of this Title, a person is not

1 disqualified for employment under this section solely because  
2 of such person's employment or representation of a creditor  
3 unless there is an objection by another creditor' -- and there  
4 was -- 'or the United States trustee' -- and there is -- 'in  
5 which case the Court shall disapprove such employment' --

6 **THE COURT:** Wait a minute, wait. What creditor  
7 objected?

8 **MR. LANDIS:** Three twenty -- 327(c).

9 **THE COURT:** What creditor objected?

10 **MR. LANDIS:** It was a limited opposition to the  
11 debtor's application to employ and retain Ray Quinney, and the  
12 objection was filed by Jeffery Davidson, Frank Merola, Eve  
13 Karasik of Stutman Treister and Glatt, and I believe there is  
14 also an additional limited objection on behalf of Mr. McGimsey.  
15 So those matters were in fact on file. I think in the summary  
16 that's before the Court with respect to these issues, you can  
17 identify that pleading.

18 And certainly at a minimum, there was an objection by  
19 our office, and that's what gets us here today.

20 **THE COURT:** Okay.

21 **MR. LANDIS:** The status and agenda for the May 18th,  
22 2006, hearing.

23 **THE COURT:** No, no, I appreciate that -- Oh, you're  
24 right, Mr. McGimsey did object. Okay, you're correct.

25 **MR. LANDIS:** McGimsey Family Trust, May 2, docket

1 number 68.

2 **THE COURT:** You're right, correct.

3 **MR. LANDIS:** So there were objections by creditors.  
4 There was an objection by our office. That then brings into  
5 play the last clause of Section 327(c), in which case the Court  
6 shall disapprove such employment if there is an actual conflict  
7 of interest.

8 So what we're dealing with at this point in our  
9 discourse, your Honor, is simply this: Does an actual conflict  
10 of interest exist? Because if an actual conflict of interest  
11 exists, then the employment shall be disallowed. That's what  
12 the Code says. That's the fundamental premise of our argument.  
13 The question of whether or not it's disputed or not that the  
14 loan servicing agreements doesn't impact on that; the question  
15 is whether or not there is an actual conflict.

16 We've provided you the two factual bases upon which  
17 we premised that argument, and the factual premise comes from  
18 Mr. Alison's declaration itself. And we asked the Court in  
19 connection with its consideration of this opposition to look at  
20 that application closely, because it establishes the existence  
21 of a loan servicing fee obligation and it also establishes that  
22 USA Commercial Mortgage believes that people were paid interest  
23 on non-performing loans, and as a result, they got paid money  
24 that they should pay back to USA Commercial Mortgage.

25 That makes a claim against folks who got interest

1 payments on non-performing loans, and the two funds got paid  
2 money in connection with non-performing loans. Certainly, at a  
3 very minimum, they hold a bunch of non-performing loans. That  
4 isn't disputed either.

5 So to the extent that there is --

6 **THE COURT:** Well, though if I find today -- if you  
7 make me find that or suggest that I have to find that the  
8 attorneys are disqualified, doesn't that also mean that we then  
9 have to disqualify Mr. Mesereaux as to the other entities? And  
10 now we really do have a multiplication of fees?

11 **MR. LANDIS:** Well, your Honor, that's an issue that  
12 we can certainly address at another time, but what the question  
13 is here is counsel, because counsel gives legal and substantive  
14 advice to these debtors, whereas Mr. Alison's function as a  
15 general proposition, A, has been the subject of a first-day  
16 motion that this Court allowed on a limited basis, and I think  
17 providently so; and B, really what he has done and he is doing  
18 is forensic efforts to determine just what dollars are owed  
19 where. The question of what advice he gives then to the  
20 various entities that he represents may in fact create a  
21 conflict of interest, but that's a fight for another day.

22 What we're talking about here is who ought to  
23 represent the debtor entities, and will they really get  
24 independent advice from that entity? And that's the focus of  
25 our objection. We believe that in this particular case, an

1 actual conflict does exist based on what we agree are  
2 undisputed facts. If you agree with our position in that  
3 regard, your Honor, then under Section 327(c) the applications  
4 cannot be permitted.

5 Now, it's true, and you heard in the argument from  
6 counsel for the debtors, proposed counsel for the debtors, that  
7 it's not necessarily always a hard and fast rule. It is hard  
8 and fast if there's an actual conflict, and we believe there is  
9 and we ask the Court to so hold. If you disagree, then the  
10 question becomes: Is there a potential conflict that would be  
11 sufficiently serious and is likely to ripen at some point in  
12 the future such that the proposed retention would be improper?

13 We've given you the case law that says it's  
14 presumptively, not absolutely or per se, improper for the same  
15 attorney to be general counsel for related debtors where one  
16 debtor is a creditor of a related debtor.

17 And you asked me the question, and it was a good one:  
18 Are you telling me that in every single case where there's a  
19 parent and a subsidiary that it's absolutely impossible for  
20 there to be joint representation? If there is the absence of  
21 an actual conflict, Judge, and if the -- if in fact the Court  
22 doesn't find that a potential conflict is enough to warrant  
23 disqualification, the Court has that much discretion.

24 So in other words, the first question you have to  
25 answer is, is there an actual conflict? And if there is, the

1 inquiry ends. If there's not, you have to determine whether or  
2 not there's a potential conflict that would warrant denial.  
3 Because of the presumptive of improper representation where  
4 there is a common debt owed between multiple estates, we  
5 believe that in this particular case, even potential conflicts  
6 of interest that exist would warrant disqualification.

7           The two types of pre-petition debts we've covered.  
8 As a result, the presumptive kicks in. At an absolute minimum,  
9 a potential conflict exists between the interests of USA  
10 Commercial Mortgage Company and those of the funds, especially,  
11 your Honor, with respect to how much money was paid to the  
12 funds on non-performing loans and whether and to what extent  
13 USA Commercial Mortgage is going to seek to recover that money.

14           Additional potential conflicts of interest we  
15 identified are the \$58 million-dollar inter-company receivable  
16 that was owed by USA Investment Partners, LLC, to USA  
17 Commercial Mortgage in a very carefully crafted declaration  
18 that said, quote, 'And possibly other debtors'. Well, if that  
19 particular loan transaction wasn't properly documented, and  
20 there's the potential interest in that loan transaction in  
21 relation to other debtors in addition to USA Commercial  
22 Mortgage, the difficulty in one counsel giving independent  
23 advice to all interested parties, it's incredible, it's  
24 massive.

25           Because how can you be certain, if it's not



1 documented but you know how much it is, and it's possible that  
2 some of the interests go to the other debtors, who's to be sure  
3 that the other debtors get a fair shake? The attorney for USA  
4 Commercial Mortgage? If that's not a potential conflict that  
5 warrants this Court's careful consideration in the context of  
6 whether or not this particular application ought to be denied,  
7 I don't know what would be.

8 Two things, your Honor, in closing. The existence of  
9 a potential conflict of interest may require disqualification  
10 of a professional if, in the judgment of the Court, the  
11 conflict is sufficiently important and there is a sufficient  
12 likelihood that it will ripen into actual conflict.

13 **THE COURT:** Now --

14 **MR. LANDIS:** That's the scope of this Court's  
15 discretion.

16 **THE COURT:** Are you saying -- I just need to clarify.  
17 You're not suggesting they couldn't continue to represent USA  
18 Commercial, for example? We just have to have new counsel for  
19 the funds?

20 **MR. LANDIS:** If you find that there is an actual  
21 conflict of interest, it's prohibited. If you find that there  
22 is not an actual conflict but the potential conflicts going  
23 forward are such that continued representation is not an issue,  
24 at that point in time then I think the debtor's counsel have a  
25 decision to make from a professional standpoint.

1 I don't believe that it would be appropriate or  
2 provident to remain in a case where a conflict of interest has  
3 been identified. However, that's an issue that we will have to  
4 address in the event that counsel decides to try to remain in  
5 the case for one of the parties that it represented.

6 The real concern, Judge, is this: To the extent that  
7 they've already represented all three debtors, an awful lot of  
8 information has to have been made available to one set of  
9 attorneys, and that information is in large part financial, and  
10 is in large part the kind of information that can be used to  
11 the detriment of the other entities, and in particular, the  
12 funds.

13 **THE COURT:** But how can any of this be used to the  
14 detriment of the funds at this stage? It's all been open  
15 information. This is not a case in which there is anything  
16 hidden; how is it possible? That's not the usual -- that may  
17 be a usual case but that's not the case here.

18 **MR. LANDIS:** I'm going to respectfully disagree with  
19 the Court about the fact that there's been full disclosure. We  
20 don't even have schedules. As a matter of fact, all we've got  
21 is information that says what loans are performing and what  
22 loans aren't. When you look at the information that says what  
23 loans aren't and you identify Mr. Alison's declaration as  
24 saying that gives rise to a claim in favor of USA Commercial  
25 Mortgage against people who received interest payments on non-

1 performing loans and you see the magnitude of the non-  
2 performing loans held by the funds, I would respectfully  
3 disagree with the idea that there has been full disclosure or  
4 that there is a lack of conflict based on the record before the  
5 Court.

6 The bottom line, Judge, is this: If you disagree with  
7 our position that there is an actual conflict of interest, the  
8 question changes then to whether there is a potential conflict  
9 that would warrant denial of the application. We've pointed  
10 you to the presumptive requirement for disqualification. We  
11 recognize the Court's discretion. But we also would ask the  
12 Court to consider that the standard under Section 327 for  
13 retention of counsel is very high. If there is any doubt as to  
14 the existence of a conflict, the doubt should be resolved in  
15 favor of disqualification.

16 Judge, again, we're not adding layers of  
17 administration here because there's only going to be one lawyer  
18 for the funds, or one --

19 **THE COURT:** Right, but you have all that work that's  
20 going to have to be done to get that person up to speed;  
21 hundreds of thousands of dollars.

22 **MR. LANDIS:** And if that is --

23 **THE COURT:** You concede that, right?

24 **MR. LANDIS:** Your Honor, I can't argue the facts on  
25 dollars, but what I can argue is this: If you don't get

1 independent counsel involved for each of the independent  
2 entities in the five cases that are before you now, when the  
3 conflict do come up, and they will, if you think the cost  
4 attendant to getting up to speed in the first -- with respect  
5 to cases that have been on the docket for only thirty days is  
6 significant, the level of cost attendant to having new counsel  
7 appear six months or a year into the case is significantly  
8 higher.

9 This matter needed to be brought to the Court's  
10 attention. That's the reason for the opposition.

11 **THE COURT:** And I appreciate that.

12 **MR. LANDIS:** And for those reasons, your Honor, and  
13 understanding that there are many other substantive matters  
14 relating dollars and cents on this Court's docket, you know  
15 what we're asking your Honor.

16 **THE COURT:** Right.

17 **MR. LANDIS:** That the applications be denied.

18 **THE COURT:** Thank you, and I appreciate it. I've  
19 asked you a lot of questions.

20 Anybody have any other opposition or comments before  
21 I reply? Wait, wait.

22 **MR. MCGIMSEY:** I would like to make two, your Honor.

23 William McGimsey. I also filed an opposition, and I  
24 believe that the conflicts are blatant and already  
25 acknowledged. I won't repeat anything that Mr. Landis said, I

1 would join in him, but a couple of things that have come out  
2 through the brief 341 meetings at which, admittedly, because of  
3 time constraints, we couldn't go into everything. But for  
4 instance, USA Capital Diversified Trust Deed Fund apparently  
5 has no creditors. Probably had it had its own counsel, would  
6 not be in this Chapter 11 proceeding.

7 USA Capital Diversified Trust Deed Fund is managed by  
8 its managing member, USA Capital Realty Advisers, who simply  
9 hired USA Commercial Mortgage to service the loan agreements.

10 There is no dispute that there are loan agreements or  
11 servicing agreements in place, but there is, or should be, a  
12 significant dispute whether or not those loan servicing  
13 agreements should stay in place. I believe there is a real  
14 chance -- in fact, more than that -- that USA Capital Realty  
15 Advisers breached its agreement to properly manage the affairs  
16 of Diversified Trust Deed Fund.

17 Mr. Alison has identified the fact that USA Capital  
18 Diversified Trust Deed Fund has twenty-three loans, twenty of  
19 which are non-performing. And, as far as I can tell from  
20 whatever has been so far presented, in not one of those twenty  
21 instances is there any foreclosure proceeding going on, is  
22 there any legal particular whatsoever to attempt to collect  
23 those monies.

24 What is happening is that every month USA Capital  
25 Diversified Trust Deed Fund is now paying what we figure is

1 either a hundred and five thousand or a hundred and seven  
2 thousand which goes to USA Commercial Mortgage, which is now  
3 funding its -- partially funding its operations through that  
4 hundred and five thousand dollars. That hundred and five  
5 thousand dollars has nothing to do with what kind of job USA  
6 Commercial Mortgage or USA Capital Realty Advisers does for the  
7 fund. It is based as a percentage of the funds that are being  
8 managed. So --

9 **THE COURT:** But that was the agreement?

10 **MR. MCGIMSEY:** That was the agreement, that was the  
11 agreement, and I don't question that, but I think the funds  
12 have been totally mismanaged, and so there is a real question,  
13 one, why is USA Capital Diversified Trust Deed Fund in this  
14 proceeding at all? And, if it has its own attorney, under the  
15 limited liability company agreement, it could change its  
16 manager, it could change, you know, I mean it could bring an  
17 action to get out of this loan servicing arrangement.

18 Now, that might not be the best thing, but that's  
19 going to be -- But these attorneys, you know, how do they say  
20 it? I mean how do you give advice to Mr. Alison as to whether  
21 or not this \$58 million dollars which he's attempting to  
22 collateralize from the former principals, as far as I've heard,  
23 that's going to be collateralized in favor of USA Commercial  
24 Mortgage. Well, maybe it should be collateralized in favor of  
25 Diversified Trust Fund or Capital First Trust Deed. How do we

1 decide that?

2 And one of the things that with regard to that \$58  
3 million dollars that Ms. Jarvis indicated, she said, well, it's  
4 an accounting issue. When that comes out, it won't be subject  
5 to dispute. Well, it won't be subject to dispute if they all  
6 have the same attorney.

7 **MR. GARMAN:** Your Honor, I didn't file an opposition,  
8 so with the Court's indulgence I'll be brief, because  
9 circumstances have changed in the last twelve hours that have  
10 changed our position on what's happening.

11 Your Honor, let me tell you -- I represent a couple  
12 of --

13 **THE COURT:** Tell me again who you represent.

14 **MR. GARMAN:** I represent a couple of direct lender  
15 clients who are long-standing clients of the firm Higgins and  
16 Buckalew. In addition to that, we were contacted by hundreds  
17 of direct lenders, representations we have never accepted, who  
18 actually provided us hundreds of thousands of dollars in order  
19 to represent their interests.

20 We didn't think an official committee of direct  
21 lenders could be formed in this case initially. We support the  
22 fact that it has now been formed, and we've told those people  
23 we think that the collective wisdom of the committee is where  
24 you need to be led now, and as such, we are in the process --  
25 excuse me, of returning all of those retainers that were

1 provided to us. And again, we didn't accept the  
2 representation.

3 That was premised upon an assumption that the direct  
4 lenders would have an independent voice, and it's Mr. Merola  
5 and Stutman's employment application for both the direct  
6 lenders and the funds that now cause our existing clients  
7 grief.

8 We had anticipated that there were potential  
9 conflicts of these debtors. At the end of the day, we can all  
10 talk about accounting now, but I remember you told me very  
11 early in my career: Follow the money. And in this case, \$950  
12 million dollars is at stake. Eight hundred million of it is  
13 the direct lenders' money.

14 The question everyone is dancing around at the moment  
15 is 541; is it property of the estate? If you read the debtor's  
16 motion to hold the funds, they have headings, and in four pages  
17 of points and authorities, they may argue it's their money in  
18 the future, but they haven't decided to do so. Thus, the  
19 potential conflict that exists between fund members and direct  
20 lenders.

21 At the end of the day, is the direct lenders' money  
22 going to be brought into this estate to pay the claims on a  
23 pro-rata basis, as the debtor insinuates may happen? That's  
24 the conflict we've seen, and that's the conflict we've been  
25 concerned about. That's why I didn't think an official



1 committee of direct lenders was possible, because we thought  
2 the direct lenders would come to court, as our clients have  
3 insinuated, and say, 'No, we're the lender, we're not in  
4 bankruptcy, the borrower is not in bankruptcy; only the  
5 servicer is, and as such, this isn't property of the estate.'  
6 Well, if they're not property of the estate, I don't know how  
7 you talk out of the other side of your mouth and decide that  
8 you're going to get paid from the estate. That's been  
9 resolved, and we think that it was resolved to the benefit of  
10 direct lenders, because we think they should speak with a  
11 common voice. Otherwise, this process breaks down.

12           Having said that though, ninety days from now we're  
13 fighting between the fund members who have a disproportionate  
14 number of bad loans, because there was no oversight by direct  
15 lenders on those loans. Hant Ges and Milanowski had free rein  
16 to invest those funds in what they wanted, and the direct  
17 lenders who did their own due diligence on each of these  
18 projects. If the direct lenders' counsel is able to advocate  
19 that their property, the loans, their direct funds, did not  
20 constitute property of the estate, we envision that that was a  
21 scenario in which these potential conflicts could be addressed  
22 and that you would have adequate representation on all sides.

23           The problem is, is that we anticipate it's fairly  
24 likely that the debtor is going to advocate that the direct  
25 lenders' proceeds constitute property of the estate. And if

1 you have one set of counsel representing both fund members  
2 whose interest it is to bring in those direct loans and  
3 representing the direct lenders, you don't have that  
4 independent voice speaking to this critical -- it will be the  
5 key issue in this case. Do the direct lenders' funds  
6 constitute property of the estate? Every decision you make is  
7 going to be premised upon that.

8 And let me give you an example. The term sheet that  
9 you have before you today contemplates all property of the  
10 estate will be a super priority --

11 **MS. JARVIS:** Your Honor.

12 **THE COURT:** Uh-huh?

13 **MS. JARVIS:** If I can interrupt? I really think this  
14 goes -- the argument goes not to what's before the Court today,  
15 it goes to dealing with the committees, their representation,  
16 their, you know, their formation and --

17 **MR. GARMAN:** Your Honor --

18 **MS. JARVIS:** -- I think this really is better  
19 reserved for, you know, a later time.

20 **MR. GARMAN:** I saw a potential conflict that I  
21 thought could be resolved through a mechanism. That potential  
22 conflict exists and now it's given rise over the last twelve  
23 hours to --

24 **MR. LANDIS:** Your Honor, the matter before the Court  
25 though is only the question regarding retention of debtors'

1 counsel in multiple entities.

2 **MR. GARMAN:** Right; I acknowledge that.

3 **MR. LANDIS:** We are not only faced with nothing on  
4 file, but now we're far afield from the issues.

5 **THE COURT:** So --

6 **MR. GARMAN:** So my concern is this: Is -- There is a  
7 potential conflict here, and that conflict, I think, comes down  
8 to what constitutes property of the estate, and there's going  
9 to be a fight someday between fund members and the direct  
10 lenders.

11 **THE COURT:** Okay, thank you.

12 **MR. GARMAN:** And -- and these debtors, with one set  
13 of counsel, cannot receive independent advice as to what's in  
14 the best interest of their constituents. And in the case of  
15 USA Capital, those may be the direct lenders. In certain  
16 instances of the funds, they may be hearing conflicting  
17 positions. The fund members are going to want to bring all  
18 these assets in. I think that goes without saying.

19 It arises in issues you're dealing with today. It  
20 arises in issues that the debtors are undertaking now. As an  
21 example, the debtors are going out trying to get secure loans  
22 from Hant Ges and Milanowski for unsecured loans they were  
23 provided. That sounds like a great idea. I think that it  
24 supports and is in the best interest of many of the  
25 constituents they represent. But many of the direct lenders

1 were specifically induced into loans because they were provided  
2 personal guarantees on identifiable loans by Hant Ges and  
3 Milanowski. Well, it may benefit the funds to bring these  
4 assets into the estate, and it may benefit certain creditors  
5 and/or direct lenders, but at the end of the day, people need  
6 to have independent advice as to what constitutes the best  
7 interest for each of the constituents. Now --

8 **THE COURT:** Well, that's why they get their own  
9 attorneys.

10 **MR. GARMAN:** I agree.

11 Now, nobody wants to tack on millions of dollars of  
12 additional fees, but, your Honor, we're dealing with nearly a  
13 billion dollars. An additional one million dollars, which is a  
14 sizable sum --

15 **THE COURT:** But you and all your clients are claiming  
16 it's not a billion. You and your clients are all claiming  
17 that's my money.

18 **MR. GARMAN:** Well, that's seven --

19 **THE COURT:** All we get is --

20 **MR. GARMAN:** That's \$800 million --

21 **THE COURT:** No, but the point is your clients are  
22 saying that billion dollars, of that billion, only, what is it,  
23 twelve percent belongs to the estate. The billion belongs to  
24 your clients.

25 **MR. GARMAN:** That's right, your Honor, but it's still

1 a billion dollars that's being -- that people are fighting  
2 about.

3 **THE COURT:** So are your clients willing to be  
4 surcharged?

5 **MR. GARMAN:** I don't think anybody wants to be  
6 surcharged, but it's a dialogue that has to take place. And  
7 when we're talking about sizable numbers like that, a million  
8 dollars out of a billion is one tenth of one percent. And it's  
9 still a million dollars of course, and it's a large sum of  
10 money.

11 But the problem comes down to you can't have a  
12 situation where the funds and those who are supposed to  
13 represent the direct lenders, and in this case those are two of  
14 the debtors, or three of the debtors, aren't getting advice  
15 specific to the creditors or direct lenders of their group.

16 **THE COURT:** Okay, we need to move on. It's 11:00  
17 o'clock, I've got four more hearings.

18 **MR. GARMAN:** Sure.

19 **THE COURT:** I've got a noon meeting.

20 **THE COURT RECORDER:** Say your name.

21 **MR. MASON:** Richard J. Mason on behalf of Dr. Gary  
22 Kantor who is one of the substantial investors. Judge, I'll  
23 try to be very brief.

24 **THE COURT:** Is he an investor in the fund or is he  
25 what we call a direct lender or both?

1           **MR. MASON:** All, all of the above, your Honor.

2           And it's Dr. Gary Kantor's judgment that to the  
3 extent that the Court has discretion in this matter, that we  
4 would be better off with a single counsel for the debtors, a  
5 single chief executive or restructuring officer for the  
6 debtors.

7           We recognize the arguments of the United States  
8 trustee. Mr. Landis is doing a very good job of trying to keep  
9 an eye on the conflicts here. I am confident that if an actual  
10 conflict arises, he will be the first to bring it to the  
11 Court's attention.

12           Counsel for the debtor has indicated that at the end  
13 of the ninety days when Mr. Alison has a better view of the  
14 financial condition of each of these debtors, if there are  
15 conflicts, either conflicts counsel will have to be appointed  
16 or there will have to be some kind of a new arrangement.

17           Your Honor, as you well know, if you deny this  
18 motion, we'll have to have multiple lawyers, multiple  
19 executives, multiple -- the disputes in this case will increase  
20 geometrically. To the extent that your Honor has discretion,  
21 and I believe even the United States trustee has acknowledged  
22 that you have discretion, because the conflicts are potential  
23 conflicts only, we would urge your Honor to grant the motion  
24 with the protections that have already been offered by debtors'  
25 counsel. Thank you.

1           **THE COURT:** Okay. All right, reply?

2           How do you intend to deal with this motion that's  
3 coming up on the 5th -- sorry; yes, the motion that's coming up  
4 on the 5th -- to temporarily hold funds? Wouldn't that motion  
5 -- wouldn't the fund perhaps have a different view point than  
6 the mortgage company?

7           Now, on one hand you could say the fund would want  
8 that to happen because, while they may want their monies, by  
9 the same token they don't want the direct lenders to get their  
10 monies until we sort it all out. So, you know, you can't say  
11 'Don't take mine but -- Give me mine but don't take theirs.'  
12 But doesn't that sort of present a problem?

13           **MS. JARVIS:** Well, it applies across the board, you  
14 know, in the sense that it's a temporary request, just while we  
15 sort things out. And again, through that ninety days, to see  
16 if there are actually any conflicts or any problems that would  
17 cause some divergent interests.

18           I mean the issues that were just raised with respect  
19 to the direct lenders really are not issues that are between  
20 the debtors. They're between the debtors and the direct  
21 lenders, but the direct lenders are not being represented, you  
22 know, by the debtor. I mean they have separate counsel. So  
23 he, you know, raised some possible conflicts, but they're not  
24 between the debtor entities themselves. I don't think they're,  
25 you know, that the issues that have been raised so far with

1 respect to the motion to hold the funds have been all raised by  
2 the direct lenders, not by the funds themselves.

3 But again, it's temporary. It's not, you know, we've  
4 raised some possible, you know, solutions or end games that may  
5 come out in this case. We're hoping that the end game is  
6 everybody just gets their principal and interest as they  
7 anticipated, and that certainly is our goal to move towards  
8 that. We raised that only for purposes of, you know, we just  
9 need some time to sort that out. And I think in the interim,  
10 there is, you know, no conflict that has been identified. What  
11 we're talking about now is a lot of speculation, a lot of  
12 speculation, but no real actual dispute that currently exists  
13 that would cause disqualification.

14 And, you know, we have offered to, and maybe we'll  
15 just go forward in order to try to kind of move this along and  
16 anticipate in case there is any problems, you know, hiring  
17 conflicts counsel that could separately advise the funds to the  
18 extent there are some issues that come up between us. But I  
19 think where there has been, you know, no actual conflict, no  
20 actual dispute, it's all speculation, that it's not appropriate  
21 for disqualification in this instance.

22 And remember that we talked about this case. This is  
23 really a case about a hundred and fifteen loans. And, as your  
24 Honor noted, the vast majority of those are like Dr. Kantor, or  
25 the vast majority of the investors in this case are like Dr.



1 Kantor in that they are in all three investments. And when you  
2 look at those a hundred and fifteen loans, because they involve  
3 everyone, there is a common interest, and that really doesn't  
4 create a conflict to deal with, you know, pursuing collections  
5 and facilitating those loans which are being serviced by  
6 Commercial Mortgage for 200 to 300 investors per loan.

7 So the fact that there are, you know, some, again,  
8 speculations that there could be some differences is not basis  
9 for disqualification.

10 And even with respect to the *Interwest* case; like I  
11 said, this is not in this district, but even that case does not  
12 say that when you have, you know, debts between affiliates,  
13 which frankly almost all affiliates have some debts. Usually  
14 they have a common cash management system where they are not  
15 disputed, and right now that's all we've got is not disputed,  
16 you know, ordinary course transactions between the debtors.  
17 That does not require disqualification.

18 And that's recognized by 327(c), because, if there  
19 was -- if the existence of those inter-company debts in and of  
20 itself was a disqualification, which is I think what the U.S.  
21 trustee is arguing, then the Court wouldn't have to make the  
22 determination that there was an actual conflict of interest.  
23 And that's what 327(c) says, is that that only is disqualifying  
24 if there's an actual conflict of interest, and no actual  
25 conflict has been identified.

1           There's no dispute, you know, as was recognized under  
2 the authorities that define actual conflicts of interest. It's  
3 all speculation, and that is not an appropriate basis at this  
4 point in time to disqualify us.

5           **THE COURT:** Okay.

6           Mr. Merola, do you have a comment; I forgot to ask?  
7 I mean if you don't, that's fine.

8           **MR. MEROLA:** Your Honor, the issue about 327 versus  
9 328 we think has been adequately addressed and we'll deal with  
10 the comments of Mr. Garman a little later on the calendar.

11          **THE COURT:** Okay.

12          **THE COURT:** All right, I'm going to grant the motion  
13 to retain for ninety days -- Well, let me go back. I find  
14 there is no actual conflict of interest, so they shall not be  
15 disqualified. But I want to review this at the end of the  
16 ninety days because I do see potential conflicts on the  
17 horizon.

18           For example, I mentioned the potential conflict on  
19 this temporarily hold funds. But again, I don't think that's a  
20 conflict because I said on one hand, it represented the fund,  
21 you could argue -- one could argue, no, I don't want you to  
22 hold the monies back; I want the money now. But the opposite  
23 part of the motion is that if that's the case, then that means  
24 all the direct lenders have to be paid their money too, and it  
25 may well be the direct lenders got paid more than they should

1 have gotten paid. Nobody knows at this stage. We're all  
2 speculating.

3 I think there will be conflicts in the future, and I  
4 think that we need to look forward to getting separate counsel  
5 for the funds.

6 Another reason I don't find -- Well, there are no  
7 actual conflicts now. I don't find the fact that there's a  
8 servicing agreement to create an actual conflict. And  
9 potential conflicts, we are a stage now where, you know, for  
10 example, just by the very nature of a servicing agreement, the  
11 point is you all act together to get the money in, and then  
12 maybe later you're going to fight about who gets the money.

13 Let's just assume, for example, we had just USA  
14 Commercial Mortgage with nothing but direct lenders, and let us  
15 assume that we had one of those situations where it was a 120  
16 percent. The point is everybody wants the money and now  
17 there's no conflict, but then there might be fights inter se as  
18 to who got the money. So I don't find there's the conflicts  
19 now; I do see potential.

20 And I am concerned, just to give the U.S. trustee a  
21 heads up, I am concerned about one committee representing the  
22 direct lenders as well as the investors and the members in the  
23 LLCs. I don't know enough about it; I'm concerned. Maybe  
24 that's not the case.

25 The other anomaly is it's on one hand easy. I was

1 thinking, well, you know what, let's just do get separate  
2 counsel for the funds now. Let's assume it wouldn't cost that  
3 much. But I'm thinking wait a minute, who are they going to  
4 report to? Mr. Alison is only one person, so we're operating  
5 in the fiction that they represent a debtor but they'd have  
6 nobody to report to. They would in essence be the philosopher  
7 king, which all the attorneys want to be anyway, but, so it  
8 would be a fiction, and an expensive fiction most importantly.

9 I think significantly we do have -- we will have  
10 committees that represent these very interests, so we'll have a  
11 side view. I do think it is very important to review at the  
12 conclusion of the ninety days for the very reason we said  
13 Mr. Mesereaux and the comments of the U.S. trustee's office  
14 before. There may well be, but by that time we're going to  
15 know whether or not there are conflicts and what the issue are.  
16 At least hopefully we'll know.

17 I appreciate the U.S. trustee, and even though I gave  
18 Mr. Landis a hard time, I appreciate the fact that, A, it's his  
19 job, and this is an important -- you know, it's important to  
20 keep professionalism, it's important to keep these interests so  
21 that everybody's interests are adequately represented. So it's  
22 an issue you needed to bring, and it's an important issue, and  
23 you certainly -- there's room for disagreement in this area.

24 Let's take a short break and then we'll go back and  
25 finish up the calendar.

1           **THE CLERK:** All rise.

2           **(Recess from 11:01 a.m. to 11:15 a.m.)**

3           **THE CLERK:** All rise. Bankruptcy Court is now in  
4 session.

5           **THE COURT:** Be seated.

6           Excuse me. I probably shouldn't tell you this  
7 because it'll encourage everybody to talk longer, but I'm going  
8 to skip my noon meeting, unless everybody would prefer to come  
9 back at 1:30. I assume you'd just as soon go through, correct?

10          **MR. SCHWARTZER:** Please.

11          **THE COURT:** It's okay; it's a judge's meeting, it's  
12 okay.

13          **(Laughter)**

14          **MR. SCHWARTZER:** No, I just may ask permission to  
15 withdraw at around a quarter to noon because I'm supposed to be  
16 one of the speakers at the SNABA (phonetic) luncheon today.

17          **THE COURT:** Oh, that's right, okay.

18          Oh, so can you --

19          **MR. SCHWARTZER:** But that's not a real problem. It's  
20 a Chapter 7 panel of trustees, and there are six other guys  
21 who --

22          **THE COURT:** Right.

23          **MR. SCHWARTZER:** -- are more experienced than I am.

24          **THE COURT:** And I'm sure nobody cares what you have  
25 to say anyway?

1           **MR. SCHWARTZER:** Right.

2           **(Laughter)**

3           **MR. SCHWARTZER:** Except in this courtroom where, of  
4 course, I know you wait on every word.

5           **THE COURT:** Okay, the next one's a little less  
6 controversial I hope. It's the motion concerning notice.

7           **MR. SCHWARTZER:** Yes, your Honor. This is pretty  
8 much a standard motion for an order limiting notice. And  
9 basically what it says is that we want to provide notice to the  
10 committees, committees' counsel, to the government agencies  
11 involved, and anyone who files a request for notice. So any of  
12 these investors who want to get notice of every single paper we  
13 file, they can get it.

14           On the other hand, we're hoping, because there are  
15 like some 6,900 entities involved in this case, that by  
16 limiting notice to only this group, the standard group, plus  
17 people who specifically request, it will be a cost-saving  
18 matter for this bankruptcy estate.

19           **THE COURT:** I would also like to see you add, and  
20 maybe it's covered, is that if you have a motion that affects a  
21 particular loan, that all the individuals, all the entities  
22 and/or individuals who are lenders on that loan be noticed.

23           So for example, today's motion, since you've had all  
24 those particular loans involved, you would have had to notice  
25 those people. But I think that, A, is a due process issue, and

1 -- well, more importantly, a due process issue affecting a  
2 specific loan.

3 **MR. SCHWARTZER:** Okay. With regard to -- I see. You  
4 mean like on the motion that we're saying we want to have  
5 authority to give releases on loans --

6 **THE COURT:** Yes.

7 **MR. SCHWARTZER:** -- and we don't know which ones?

8 **THE COURT:** If it affects a specific loan.

9 **MR. SCHWARTZER:** Okay. Yes, your Honor, I could  
10 amend the order -- to prepare an order that provides where we  
11 have a motion that affects a specific loan, that all the  
12 investors in that loan be noticed.

13 **THE COURT:** Right. And I saw some limited  
14 opposition. Did you work out those additional --

15 **MR. SCHWARTZER:** Well, actually, the committee --

16 **THE COURT:** -- or comments?

17 **MR. SCHWARTZER:** The committee wanted us to limit  
18 notice even more. We included in the people we were giving  
19 notice to each party who was on the list of twenty largest  
20 investors for the fund -- for each of the two funds and for the  
21 direct lenders. The committee said as long as there's a  
22 committee, you don't have to do that. It's up to the  
23 discretion of the Court on that.

24 **THE COURT:** I think you might as well; it's just  
25 forty more notices.

1           **MR. MEROLA:** It's eighty more, your Honor, of  
2 everything.

3           **THE COURT:** Oh, eighty more.

4           **MR. SCHWARTZER:** And it's written notice because  
5 these people don't necessarily have e-mail addresses, so  
6 they're not getting their notice automatically.

7           **THE COURT:** And there are committees for each of  
8 these three now?

9           **MR. SCHWARTZER:** Yes, there are.

10          **THE COURT:** Okay. All right, so we can eliminate  
11 that then.

12          **MR. SCHWARTZER:** Okay.

13          **THE COURT:** Because of course any individual can file  
14 a request for special notice.

15               May I suggest that when you send -- Now, you're going  
16 to send this out to everybody, right?

17          **MR. SCHWARTZER:** Yes, your Honor.

18          **THE COURT:** Why don't you prepare a form so that it's  
19 one form, and let's have -- Is Mary Ann still in here? Mary  
20 Ann Street still in here?

21          **THE CLERK:** No, I don't see her, your Honor.

22          **THE COURT:** Should we have BMC, because it's going to  
23 affect the mailing matrix?

24          **MR. SCHWARTZER:** That's correct.

25          **THE COURT:** Does BMC monitor the mailing matrix?



1           **MR. SCHWARTZER:** Actually we create and file the  
2 master mailing matrix, and we're continually updating it, and  
3 we provide it to BMC Group when there's going to be a mailing.

4           **THE COURT:** Okay. Let me suggest this in a request  
5 for special notice; that you put in there -- if they request  
6 special notice A and B, does this address supersede any prior  
7 addresses.

8           **MR. SCHWARTZER:** And could we also ask them if they  
9 can get the notice by e-mail?

10          **THE COURT:** Yeah.

11          **MR. SCHWARTZER:** Because that really does save a lot  
12 of --

13          **THE COURT:** I don't think there's a problem with  
14 that.

15          **MR. SCHWARTZER:** -- a lot of effort, and in this  
16 group of investors, I think there's a lot of computer-savvy  
17 people.

18          **THE COURT:** Yeah. And I think -- I don't think  
19 there's any problem with the federal rules that prohibit that.

20                So we could accomplish two things here. Now, let me  
21 just give you my view of a request for special notice. My view  
22 of a request for special notice, all that means is if you're  
23 entitled to notice, that's the address it goes to. My view of  
24 the rule is not that if you weren't entitled to the notice,  
25 you'd get it anyway. But if the debtor feels it's easier just

1 to send it to everybody regardless of -- without thinking about  
2 who has to get the notice, that's fine by me.

3 **MR. SCHWARTZER:** That's what we've been doing, your  
4 Honor.

5 **THE COURT:** Okay.

6 **MR. SCHWARTZER:** That would be the intent of this  
7 order, would be if you file a request for notice, you will get  
8 notice of every -- every paper that we file, we will send out  
9 to those people, either by electronically, if they've given us  
10 an electronic address preferably, or by first-class mail.

11 **THE COURT:** Now, let's see, they would not have filed  
12 their proofs of claim or interests yet.

13 **MR. SCHWARTZER:** No, they would not, your Honor.

14 And one of the things you have to recall in this  
15 case, until we do the accounting --

16 **THE COURT:** Right.

17 **MR. SCHWARTZER:** -- we don't want to send people the  
18 forms to spell out their notice.

19 **THE COURT:** That's right. We've extended the bar  
20 date on this, have we not?

21 **MR. SCHWARTZER:** Yes, we have.

22 **THE COURT:** So that's true. So when you send out  
23 those forms, you could indicate in those forms, you know, is it  
24 really this address you wanted, the request for special notice,  
25 so we have -- so we don't have all these duplicates.

1           **MR. SCHWARTZER:** Right.

2           **THE COURT:** I don't think anybody wants duplicates of  
3 anything.

4           **MR. SCHWARTZER:** As a matter of fact, we got some  
5 pretty nasty letters about 'You must be wasting our money  
6 because we got five copies', and the problem was on the first  
7 mailing we did not have joint administration, so we were  
8 required to send five copies if we didn't know which entity --

9           **THE COURT:** If you had asked, I would have let you  
10 send one copy.

11          **MR. SCHWARTZER:** I am -- And we sent one notice.

12          **THE COURT:** Okay.

13          **MR. SCHWARTZER:** We created one notice, but --

14          **THE COURT:** Well, you've also got the problem on some  
15 of these loans, these people are wearing different hats.

16          **MR. SCHWARTZER:** That's right. For example, we have  
17 a lot of people who have the investment in their own name, a  
18 family trust, an IRA, a 401-K, and some Keogh plan, so they're  
19 getting five notices because they're five separate entities.

20          **THE COURT:** So, may I suggest --

21          **MR. SCHWARTZER:** We hope we're going to limit that.

22          **THE COURT:** So I suggest in your request for a  
23 special notice form, give some thought to devising the form  
24 such that you get as much information as you can so that you're  
25 not doing more duplicates than you need to and you find out

1 what -- you know, maybe people do want it sent to two separate  
2 addresses if they're wearing different hats.

3 **MR. SCHWARTZER:** Okay. We'll do that, your Honor.

4 **THE COURT:** And any form is acceptable to me.

5 Okay, so that is approved. So the list will be --  
6 Notice will be limited to the U.S. trustee, unsecured creditors  
7 committee's counsel, any other committee. Well, it would be  
8 the specific committees now.

9 **MR. SCHWARTZER:** Yes.

10 **THE COURT:** Secured creditors and their counsel.

11 Are we still doing -- We're not doing that to  
12 unsecured twenty anymore?

13 **MR. SCHWARTZER:** No.

14 **THE COURT:** Nor the top twenty in Diversified Capital  
15 or USA Commercial; governmental entities, those who file  
16 request for notice, and those entities who have an interest in  
17 a specific piece of property which is affected specifically by  
18 a motion.

19 **MR. SCHWARTZER:** Okay.

20 **THE COURT:** And I apologize for too many 'specifics'.

21 **MR. SCHWARTZER:** I will make something that I think  
22 everybody can use.

23 **THE COURT:** Okay, great. Okay, thank you.

24 All right, the next one we have is the return to the  
25 investors in the Bundy Canyon Project?

1           **MR. SCHWARTZER:** Yes, your Honor. And with regard to  
2 that, we didn't receive any objections, but I just want to make  
3 --

4           **THE COURT:** I do have an opposition; Mr. Kinas'.

5           **MR. SCHWARTZER:** I thought it was a joinder that I  
6 saw. If there's an opposition, it must be late-filed, your  
7 Honor.

8           **THE COURT:** Maybe I misread it.

9           **MR. SCHWARTZER:** Oh, that's right. Mr. Kinas is  
10 withdrawing his opposition.

11          **THE COURT:** Oh, okay.

12          **MR. KINAS:** Yes. Your Honor, Robert Kinas for Snell  
13 and Wilmer on behalf of JM (phonetic). We had received some  
14 information from a direct lender thirty-eight hours ago,  
15 brought that to the debtor's attention; they have provided us  
16 with additional documents, and they're in a different Bundy  
17 loan and some funds might be sequestered, so we're withdrawing  
18 the objection at this point.

19          **THE COURT:** Okay.

20          **MR. KINAS:** Thank you.

21          **THE COURT:** All right. So --

22          **MR. SCHWARTZER:** Let me -- I just want -- Even though  
23 it's not opposed, I want the Court to understand.

24          **THE COURT:** Right, exactly what's going on.

25          **MR. SCHWARTZER:** The Bundy Canyon loan was -- it's

1 actually the phase six Bundy Canyon loan. The money was raised  
2 from investors. It was actually put with a title company in  
3 California. It went through the investor trust account to this  
4 account, and these loans were collected for this specific loan.  
5 They're completely identifiable; there's no question.

6 We are suggesting in this that what we'll do is just  
7 return these monies to these investors. We know exactly who  
8 they are. The money has never been invested.

9 **THE COURT:** And indeed you're required to by Nevada  
10 law, correct?

11 **MR. SCHWARTZER:** We believe that's -- we believe we  
12 are, but I want to make sure that you understand that it's  
13 slightly different than the situation we have with other people  
14 who have money that are in the investor trust account.

15 If you recall at the beginning of this case, we had  
16 that chart, and it had one chart showing the investor trust  
17 account with money coming in, and then we had the --

18 **THE COURT:** Right.

19 **MR. SCHWARTZER:** -- collection account on the other  
20 side? This is the investor account. We have about one -- And  
21 besides this money, the Bundy Canyon money is at a title  
22 company, but in the investor trust account, there is about \$1.9  
23 million dollars. That money is there because there are some  
24 investors who are buying other investors' positions and loans  
25 and there's money owed to investors who sold their positions

1 and loans and in theory transferred it to other investors.

2           The problem we have is when you file the Chapter 11  
3 and stop it, you stop it in mid-stream. So we have two groups  
4 of people asking for the money in that. We have people who  
5 said 'I sold my interest; I want my money out', and there are  
6 people who have said 'I bought an interest but I didn't get it  
7 yet; I want my money out'. The problem is that means you have  
8 \$3.8 million dollars in claims against this \$1.9 million  
9 dollars.

10           At some point in time, this Court is going to have to  
11 determine, after we file the appropriate motion and have done  
12 the appropriate investigation, who gets that money, whether --  
13 and in which situation; which investors who already should get  
14 the money out and which investors still have the investment in  
15 the loans; are still direct lenders and still have an interest  
16 in loans that are outstanding.

17           That situation, we're not asking you to rule on that.  
18 We're just saying on the specific money that was raised for  
19 Bundy Canyon, that is very clear, no question about it, we know  
20 it was a loan that wasn't made; therefore, the money is  
21 required to be returned under Nevada law.

22           **THE COURT:** Right. And I understand that from the  
23 pleadings. Again, this money is money that's specifically  
24 identified in a trust account -- a separate trust account at a  
25 title company?

1           **MR. SCHWARTZER:** Yes.

2           **THE COURT:** All right, so that's approved.

3           **MR. SCHWARTZER:** Thank you, your Honor.

4           **THE COURT:** Just as a collateral issue on what you  
5 just suggested; may I suggest what you may need to think about  
6 to tee that other issue up is just to file an adversary  
7 proceeding, because it's in essence in the nature of an  
8 interpleader, rather than sticking these things on a motion.

9           **MR. SCHWARTZER:** It may be. First of all, we have to  
10 get enough facts to see --

11          **THE COURT:** Right; it's premature.

12          **MR. SCHWARTZER:** What we have is a situation, some  
13 people, there may be signed documents doing the transfer for  
14 some people; there may be signed and recorded documents for  
15 some people; there may be people who thought they bought  
16 something but there are no signed documents at all, and this  
17 Court is going to have to determine how to treat each and every  
18 one of those individual systems before we could determine who  
19 gets that \$1.9 million dollars.

20          **THE COURT:** Okay.

21               Okay, next we have the partial release motion. Let's  
22 see, let's do something simple first. Let's skip that. Let's  
23 go to Fidelity.

24          **MR. SCHWARTZER:** Oh --

25          **THE COURT:** I have a stipulation on Fidelity.



1           **MR. SCHWARTZER:** Yes, your Honor. And Fidelity is --  
2 basically, Fidelity Title Company was a construction control  
3 that said we don't know if we should follow your instructions,  
4 and they wanted a comfort order. And the stipulation and order  
5 that was submitted, and I believe has already been entered,  
6 completely solved that issue. But basically it was a comfort  
7 order to allow the debtor to operate in the ordinary course of  
8 business. There's 40 loan funds at Fidelity. They're just  
9 going to continue to disburse them as they would as basically a  
10 construction control.

11           **THE COURT:** Okay. I have now signed that.

12           **MR. SCHWARTZER:** Thank you.

13           **THE COURT:** That was just a glitch in my office.  
14 What I did was I transferred to my judicial assistant so she  
15 would take it off calendar. And then she didn't realize I had  
16 it in there and so she forgot to transfer it back to me. So I  
17 was trying to be efficient and that was the problem.

18           **MR. SCHWARTZER:** Okay. But it's --

19           **THE COURT:** Okay. Now, let's go back to the 105 and  
20 363 motion.

21           **MR. SCHWARTZER:** Ms. Jarvis will handle that motion.

22           **THE COURT:** Okay. And Mr. Schwartzer, if you need to  
23 leave to do that seminar, I don't have an objection. I would  
24 think that -- well, it's up to you two.

25           **MS. JARVIS:** Okay. I think it would be helpful first

1 to make sure we clarify what it is that we're asking for in  
2 this motion. What we have here is there are nine specific  
3 loans where these are loans made on projects that have  
4 condominium developments, I think timeshare developments;  
5 whereas these are resold in the documents itself, in the loan  
6 documents themselves, as these developments are sold to the  
7 ultimate buyers there is, you know, a release -- a partial  
8 release given so that the sales can go forward and those monies  
9 can come in. And then there is a mechanism in the loan  
10 agreement with respect to those monies coming back into or  
11 being collected by Commercial Mortgage as the servicer and then  
12 distributed. In the absence of a bankruptcy it would be  
13 distributed then to the lenders on that loan.

14 What is asked for is the ordinary course practice,  
15 which has occurred in the past, which is that Commercial  
16 Mortgage as the loan servicer can give these partial or full  
17 releases in exchange for these monies that come in that are  
18 defined by the loan agreement in order to enable the property  
19 to be sold and the money to be collected.

20 We are not asking for anything other than this money  
21 to be collected and put in the collections account. As we've  
22 previously explained to your Honor, we do have a segregated  
23 collections account where all monies collected on loans are  
24 put. They are accounted for separately, as those monies go  
25 into that account so we can identify them by loan as to what

1 went in. Nothing has been or will be taken out of that account  
2 except with respect to what was authorized in the cash  
3 management motion, and that involved the servicing fees and  
4 other fees that Commercial Mortgage is allowed.

5 So by bringing this money in and putting it in this  
6 account no investors' rights are being affected because this  
7 money is collected and basically accounted for. And so there  
8 is no intent to affect those rights.

9 There have been several objections filed.

10 **THE COURT:** Let me ask first. This may get ahead of  
11 the objections. Let's just go through each of these while  
12 we're at it. I think --

13 **MS. JARVIS:** And I might say, your Honor --

14 **THE COURT:** Page 14 is -- Paragraph 14 is that the  
15 first loan? Does that describe the first loan?

16 **MS. JARVIS:** Yeah.

17 **THE COURT:** I'm sorry, 13. It's going to be the same  
18 question with respect to each. Maybe Mr. Allison is the person  
19 that could answer.

20 **MS. JARVIS:** Yes, 13 is the first one.

21 **THE COURT:** Okay. So with respect to this loan are  
22 we confident that (a) all monies that had been paid -- that all  
23 monies that are condition precedent to release had been paid  
24 and that the debtor is not otherwise in default?

25 **MS. JARVIS:** Let me kind of walk you through it.

1           **THE COURT:** Okay.

2           **MS. JARVIS:** It would be helpful. It's because the  
3 one -- there were several objections filed. I don't know  
4 whether -- the only objector -- well, there are two objectors I  
5 could identify that were affected by these nine loans. I'm not  
6 sure about the others, so let me just take the Roam  
7 Development, which is 21, because that is the Walch Trust. I  
8 had identified that as one loan that they were involved in.

9           **THE COURT:** Okay.

10          **MS. JARVIS:** Okay. So what that states is you get a  
11 partial release -- these are condo units -- and they are  
12 required to pay over 90 percent of the proceeds of the sale of  
13 the condo, and there's a minimum price that they have to meet  
14 for various condos. And if they do meet that, if they sell for  
15 the minimum price and they turn over 90 percent; which would,  
16 of course, be put into the title company escrow and 90 percent  
17 would be released to us, then they are entitled to the release.  
18 And so there is a mechanism for making sure that these  
19 conditions are met.

20          **THE COURT:** But I guess what I'm saying is do we know  
21 that, for example, that there haven't been any prior units  
22 released for which they hadn't met the conditions precedent?

23          **MS. JARVIS:** We don't know that for certain.

24          **THE COURT:** Okay.

25          **MS. JARVIS:** We do know that anything that's happened

1 since Mr. Allison has been in the conditions are being met.

2           **THE COURT:** So wouldn't you have to check first to  
3 make sure that, indeed, they haven't been given a release that  
4 they shouldn't have received; or are you asking for any  
5 certifications that they're entitled to the release and --

6           **MS. JARVIS:** Well, the problem is that -- it really  
7 sort of goes to benefit the buyer, you know that's buying this  
8 condominium unit. And, therefore, if you don't give the  
9 release they can't buy it because they're not going to buy  
10 something that's subject --

11           **THE COURT:** Right.

12           **MS. JARVIS:** -- to a prior loan. So the problems  
13 that may have arisen in the past -- we have no idea whether  
14 there are problems are not, because that just is not something  
15 we've been able to figure out yet -- those exist but they're  
16 not going to change one way or another.

17           **THE COURT:** Well, it will in the sense that it's true  
18 a buyer can't buy it. But if, for example, let's assume you've  
19 got a development with 100 units and let's assume that 50 units  
20 have been released but they were released for prices less than  
21 was authorized under the deed of trust. You still have a  
22 security interest in the remaining collateral to the extent of  
23 your debt.

24           **MS. JARVIS:** Right.

25           **THE COURT:** But if you now release somebody's condo

1 unit under the appropriate grounds though, you now have less  
2 security than you had before.

3 **MS. JARVIS:** Well, you really have maintained the  
4 status quo, because in a sense that whatever is done is done.  
5 And if the security has been released and the funds haven't  
6 been collected, that going forward if you comply with that  
7 you're not making the situating any worse because you're not  
8 releasing any more security except --

9 **THE COURT:** Well, you are.

10 **MS. JARVIS:** -- in exchange for the amount of the  
11 money.

12 **THE COURT:** You are. If, for example, let's assume  
13 the release price is 130,000; but let's assume the unit is now  
14 valued at 190,000. Your collateral would be worth 190,000  
15 times 50 as opposed to 130,000 times 50, what your release  
16 price it.

17 **MS. JARVIS:** But I think what you're saying though is  
18 you want to make sure -- well, but the going forward you're  
19 paying it for a fair market value. I mean is that --

20 **THE COURT:** Well, I'm just concerned that if you  
21 release your collateral -- you know, let's assume worst case  
22 scenario, okay? Let's assume that an insider had this condo  
23 project and let's assume that 50 condos were sold and -- so  
24 they can be sold and released; but only half the money was paid  
25 for the condo instead of the full release price. So again,

1 you're entitled to be paid the whole amount. But by releasing  
2 half your collateral when you should have only released a  
3 quarter of the collateral, you've reduced the remainder.

4 **MS. JARVIS:** Right. And I recognize that it's  
5 possible that could have occurred prior to this time. But what  
6 we're talking about is --

7 **THE COURT:** Right. Is there a way though --

8 **MS. JARVIS:** Is complying with the contract so that  
9 anything that is sold, you know, after Mr. Allison has been in  
10 the place we are going to make sure --

11 **THE COURT:** Right.

12 **MS. JARVIS:** -- that we get what --

13 **THE COURT:** But isn't there a way though --

14 **MS. JARVIS:** -- the lenders bargained for.

15 **THE COURT:** -- that before you issue that new  
16 release -- I understand exactly what you're saying, and I'll  
17 hear the comments. But that seems perfectly reasonable. But  
18 isn't there a way that before any of these units are released  
19 that you could make the -- it's the project owner is going to  
20 want to make sure that these sales go through because they  
21 don't get any money, their 10 percent, if you will, until the  
22 condo is sold. Couldn't you require -- Mr. Allison require  
23 them to provide evidence that, indeed, they paid -- I mean how  
24 hard is that? You have the checks, the wire transfers, in  
25 accordance with the note and deed of trust?

1           **MS. JARVIS:** With respect to all the prior sales?

2           **THE COURT:** Right, right.

3           **MS. JARVIS:** I suppose it could be done. Really the  
4 only issue really is that 10 percent. It's not the 90 percent  
5 because we're getting that. So I think what you're --

6           **THE COURT:** Well, in the past you wouldn't.

7           **MS. JARVIS:** -- talking about -- but in the past you  
8 know we -- I mean it's not going to be changed one way or the  
9 other by this sale --

10          **THE COURT:** Yeah, because you don't have much  
11 collateral any more.

12          **MS. JARVIS:** Except that you're getting what you  
13 bargained for for the collateral that you're now releasing.  
14 And if there is some problem in the past, there may be that  
15 10 percent but there's not anything that is going to --

16          **THE COURT:** You want us to talk to Mr. Allison --

17          **MR. SCHWARTZER:** Your Honor, one of the things we  
18 want to point that this Order authorizes Mr. Allison to do the  
19 releases. It doesn't require him to do the releases. If there  
20 is a prior default under the loan agreement with this  
21 particular borrower he could enforce the agreement as written.

22          **THE COURT:** Well.

23          **MR. SCHWARTZER:** But what we need in this case is a  
24 comfort order, in effect, for the title companies to accept his  
25 signature on a release.



1           **THE COURT:** Well, can we do this? Could I authorize  
2 his doing that -- and again, I'll hear these comments -- on  
3 loans which are not in default upon certification? And all it  
4 requires is a certification by him that it's not in default.

5           **MS. JARVIS:** He's okay with that.

6           **THE COURT:** Okay. All right. So with that  
7 clarification, I want to hear if there's any objections.  
8 Because that was my main question on each of these units was my  
9 main concern was has there been a default in the past and do we  
10 know where we are.

11           **MS. JARVIS:** Right, okay. And that's fine; we can do  
12 that. And the one other objection that is filed is -- or the  
13 one issue that has been raised is whether these releases can be  
14 done without having the --

15           **THE COURT:** Money actually go.

16           **MS. JARVIS:** -- borrower go -- or, yeah, the buyer  
17 pay the money directly to the lenders rather than to USA  
18 Commercial Mortgage as a servicing company. And, you know, in  
19 the past it has all come through Commercial Mortgage; that is  
20 the past practice. And I think we laid out pretty clearly in  
21 our brief, our reply brief, why this is in accordance with the  
22 loan servicing agreement and the deed of trust, which the deed  
23 of trust is referenced even in the power of attorney that has  
24 to be done in accordance with that as well as with Nevada  
25 statute where everyone would have to be done.

1 Let me just explain to you as a practical matter --

2 **THE COURT:** Hold on. I need to let Ms. Jarvis  
3 finish. Sorry, Counsel.

4 **MS. JARVIS:** Let me just explain to you as a  
5 practical matter, you know, looking at this Roam Development,  
6 this is held by I think it's 263 lenders, so it's over  
7 250 lenders. The minimum price for one of the condos or for  
8 the lowest condo is like around \$80,000. And if you took out  
9 the 10 percent, you're down to about \$72,000. If you round it  
10 off to 250 investors, you're talking about cutting checks  
11 for -- you know, if you -- a similar interest for \$288 apiece  
12 that we would have to send out to 250 lenders to get this  
13 release.

14 That's impractical and it's not consistent with the  
15 past practice and understanding between the parties as to how  
16 this is done, because it has been done through Commercial  
17 Mortgage; nor is it consistent, as we point out, with the loan  
18 servicing agreement with the deed of trust as to specifies who  
19 is to be paid, you know, directly. So this is simply not an  
20 objection that should be sustained. And again, these funds  
21 will be held in the collection account. They will be accounted  
22 for separately with respect to this loan and the lenders in  
23 this loan.

24 **THE COURT:** Okay. And your motions to ratify partial  
25 release as previously provided -- the point is you would first

1 go --

2 **MS. JARVIS:** Well, we had to -- there were some  
3 emergency situations and we had to make a decision about what  
4 to do with respect to it. So there have been a couple of cases  
5 where the releases were given in exchange for the money.

6 **THE COURT:** Okay. But we don't know whether or not  
7 there was a default or not on those.

8 **MS. JARVIS:** They were not in default, your Honor.

9 **THE COURT:** They were not in default.

10 **MS. JARVIS:** No.

11 **THE COURT:** So you made that determination.

12 **MS. JARVIS:** Yes.

13 **THE COURT:** Okay. Now, I'm sorry. Opposition or  
14 comments?

15 **MR. SANTORO:** Good morning, Judge.

16 **MS. UNIDENTIFIED:** Your name, please?

17 **MR. SANTORO:** My name is Nick Santoro. And, your  
18 Honor, I am an attorney but I am not a bankruptcy attorney and  
19 I'm not here in a representative capacity. I'm here on behalf  
20 of my own family trust. So not being a bankruptcy attorney I'm  
21 going to hope that I don't stick my foot in my mouth too badly  
22 here, Judge.

23 I filed a joinder in Gregory Walch's opposition.  
24 That's what I'd like to talk about. The debtor's motion on its  
25 face seems reasonable enough. The debtor comes to court and

1 says that we want to assure our borrowers that they can make  
2 their payments and they can get reconveyances of their deed of  
3 trust. And on its face, as I said, that seems benign enough.  
4 We want the borrowers to make the payments and they're entitled  
5 to their reconveyances.

6 The problem, your Honor, is where the money goes.  
7 The debtor wants to take these principal payments and put them  
8 in the debtor in possession collection account. They do not  
9 want to give it to the investors, the direct lenders.

10 **THE COURT:** No. I don't think it's going to the  
11 collection account. It's going to the separate -- I'm sorry,  
12 it is but the point is it's all going to be held.

13 **MR. SANTORO:** Right. But it's --

14 **THE COURT:** It's not going to be -- they won't even  
15 take their administrative expenses. It's a separate account.

16 **MR. SANTORO:** I understand, Judge.

17 **THE COURT:** Okay.

18 **MR. SANTORO:** But what they're doing is they're  
19 taking it in their name as opposed to in the typical deed of  
20 trust reconveyance situation the borrower pays off the deed of  
21 trust, the lender gets his money back. That's not what they're  
22 suggesting here. They're saying they take the money in their  
23 own name and put it in their own account and not give it to the  
24 investors. And that's where the problem is, Judge.

25 They say in their motion that they are somehow

1 entitled under the loan documents to take these principal  
2 payments, our money, in their own name. And I simply beg to  
3 differ, Judge. If we look at the power of attorney, the power  
4 of attorney document, and it says:

5 "The services to be performed are described below."  
6 Paragraph A is fairly general. Paragraph B specifically deals  
7 with this situation, Judge, which is under the deed of trust --  
8 and we're talking about reconveyances -- if you look at sub 3,  
9 this is the power that I and other direct lenders granted to  
10 the debtor:

11 To execute and deliver full and/or partial  
12 reconveyances of the deed of trust -- and that's what they want  
13 to do -- upon the payment, therefore, to the undersigned.  
14 That's not them; that's us. That's the direct lenders who  
15 signed this power of attorney. As required by the deed of  
16 trust, which payments to the undersigned -- that's us, again --  
17 are to be made directly to the undersigned in proportion to  
18 their respective interests and not to said attorney in fact.  
19 Not to them; to us. Not to them, Judge.

20 It could not get any plainer. And the problem I have  
21 with their motion is they're coming to court and telling you in  
22 a motion -- and counsel just said it -- well, under the loan  
23 documents we're entitled to take the money in our name. Well,  
24 I'm here to tell you differently. That's the authority that I  
25 and other direct lenders gave this debtor. We did not, did

1 not, authorize them to take this money and put it in their own  
2 name.

3 And here again, I'm not a bankruptcy lawyer but I  
4 have some familiarity with contract instruction, and I know  
5 that you give words in a contract their ordinary meaning; and  
6 where a contract is clear and unambiguous it must be enforced  
7 the way it is written. And it could not get any clearer than  
8 that, Judge, in my opinion, that the payments go directly to  
9 the undersigned and not to the debtor.

10 What they are really asking the Court to do, Judge,  
11 is to re-write this power of attorney and to change the  
12 authority that the direct lenders granted to them. I have  
13 serious problems with that.

14 First, it's legally impermissible to simply re-write  
15 the contract. They have cited no authority in their motion  
16 that would allow this Court or them to even argue that you can  
17 just re-write the contract. In fact, Judge, what they did was  
18 they came to court saying that the contract allowed them to do  
19 this, and that is not the case.

20 The second problem I have with this, your Honor, is  
21 that it's this very conduct, it's the violation of that  
22 provision under the power of attorney that landed this debtor  
23 in bankruptcy in the first place. They took in principal  
24 payments. I believe Mr. Allison testified to this. They took  
25 in about \$50 million of principal payments came in. They did

1 not send that to the direct lenders. They took it in their own  
2 name, which they never should have, and then about \$50 million  
3 in prepetition interest payments on non-performing loans went  
4 out the door. So that was there to protect us from the very  
5 thing that landed us in bankruptcy court.

6           The power of attorney was designed to prevent that  
7 from happening, to protect the direct lenders from  
8 USA Commercial doing exactly what it did. And I would submit  
9 to the Court it was wrong then and it is wrong now to  
10 perpetuate that. That was our main protection. They violated  
11 it before and now they want to say: Well, you know, it's the  
12 status quo.

13           Well, Judge, my position is, you know, the status quo  
14 is not always a good thing. This status quo is a very bad  
15 thing and it harmed us. And now they want to say, well, that's  
16 how we did it before; we should continue to do that now, in  
17 violation of that special power of attorney. I completely  
18 disagree with that, Judge.

19           The other aspect of this is, the other loan documents  
20 are consistent with this power of attorney. There is a note, a  
21 promissory note. And in the first paragraph it says that the  
22 note by the borrower is made in favor of those persons listed  
23 on Exhibit A attached hereto, lender. That's the direct  
24 lenders. There's an schedule attached. It has everyone  
25 according to their investment.

1           And then the next paragraph: For value received  
2 borrower promises to pay to lender, okay. Not to  
3 USA Commercial Mortgage, not to anyone else, not to some  
4 special segregated account, to lender. That was the deal both  
5 under the power of attorney and under the note. So the  
6 documents are consistent, and I think they're explicit in terms  
7 of where that money should go, Judge.

8           Now, the only thing that the debtor relies upon is  
9 some general language in the loan servicing agreement. And I  
10 would submit to the Court that there is nothing explicit in the  
11 loan servicing agreement as there is in both the note and the  
12 power of attorney, which I read to you, which allows them to  
13 take this money in their own name. Sure there's general  
14 language about they can collect money; but there's nothing that  
15 says this, the note or the power of attorney is vitiated by  
16 anything in the loan servicing agreement.

17           And, in fact, Judge, this, (indicating), is the loan  
18 servicing agreement. In Paragraph 11 it talks about the  
19 limited power of attorney. And the highlighted portion says:  
20 "No one shall be required to look beyond such declaration of  
21 agency and limited power of attorney for evidence of USA's  
22 authority hereunder." And that's what I already read to you.

23           In other words, Judge, the power of attorney trumps  
24 any of the general language in the loan servicing agreement.  
25 And I've read the power of attorney to you, and it's explicit.



1 So by its own terms whatever general language they want to cite  
2 to you in this loan servicing agreement is -- to the extent of  
3 any inconsistency is trumped by the power of attorney I read to  
4 you. No matter how they try, Judge, they can't get around that  
5 power of attorney.

6 So, in closing -- and I know that this has been a  
7 long morning --what to do. I suggest that it is not -- let me  
8 begin by saying this, Judge. The argument the debtor advances  
9 is that this is inconvenient to have this money when  
10 reconveyances are given to borrowers be put in separate checks  
11 to each of the direct lenders.

12 Well, my response is two-fold to that, Judge. First,  
13 that was the deal. Under the promissory note the lenders  
14 agreed to pay -- I'm sorry, the borrowers agreed to pay the  
15 direct lenders. And under the power of attorney USA agreed not  
16 to take the money into their own name. So that was the deal.

17 Secondly, it seems to me a little bit offensive, the  
18 concept that the convenience of the borrower somehow takes  
19 precedence over protection of their investors and direct  
20 lenders. The argument is, well, the borrower may have to write  
21 200 checks. Well, and these people in this courtroom are out a  
22 lot of money. They have a lot of money at stake here. And  
23 they want to tie it up in their account contrary to the terms  
24 of these documents. I do not think, Judge, that the  
25 convenience of either the borrower or the debtor should

1 overcome the contractual rights of the direct lenders.

2 As an alternative, Judge -- and this is where I could  
3 really be getting far afield of what I do in state court -- if  
4 the Court buys into this argument of convenience, which I  
5 don't; but if you want to look at that idea, maybe an  
6 alternative would be to open a separate bank account for each  
7 loan.

8 My understanding is there's 115 loans that USA has  
9 out there to direct lenders such as myself. So you open up a  
10 separate bank account for each one so you don't get into any  
11 commingling situation. The accounts are all for the benefit of  
12 each and every benefit lender to the extent of their  
13 proportional interest in the note and deed of trust. It's a  
14 trust account. You change the instructions with the borrower  
15 so that he wires his payment every month into that one account.  
16 This way the borrower is only making one payment. There's no  
17 inconvenience for the borrower. And there shouldn't be any  
18 other inconvenience to the debtor other than simply setting up  
19 115 separate bank accounts.

20 But our point is this, Judge. There's no way that  
21 money should go into any sort of debtor in possession account  
22 because they don't have the right to do that, I never agreed  
23 that they could do that, they violated that already. And  
24 sitting here today I have no inclination to want to expand upon  
25 the authority that we granted to this debtor after everything

1 that's happened in this case. I do not want to perpetuate a  
2 status quo that has been harmful.

3 Thank you, Judge.

4 **THE COURT:** Okay. Any opposition?

5 **MS. DAVIS:** Your Honor, I have a bit of a different  
6 issue. In addition to the partial release loans the motion  
7 asks to accept a payoff on a satisfaction of the opaque  
8 (phonetic) loan. Now, two of my clients have beneficial  
9 interest in the opaque loan. And this motion is asking to  
10 accept \$5,867,000 as apparently a satisfaction of the note.  
11 Now, the opaque loan is also something that's been listed by --

12 **THE COURT:** Isn't it a great name for a loan?

13 **MS. DAVIS:** I know.

14 **THE COURT:** I mean it's like --

15 **MS. DAVIS:** I like the Y (phonetic) names, too.

16 **THE COURT:** Yes.

17 **MS. DAVIS:** But getting back to this, your Honor,  
18 the --

19 **THE COURT:** This is on Paragraph 20. Correct. Okay,  
20 go ahead.

21 **MS. DAVIS:** Yes, yes. So the problem we have here is  
22 it's been previously listed as a non-performing loan. And, you  
23 know, let's not lose sight of all of the people who are living  
24 off of their investments in these loans. You know, we're not  
25 talking about just the borrowers and the servicers. We're

1 talking about potentially 7,000 people who are not getting the  
2 money that they previously were entitled to get.

3 We're also -- if you look at it from a bankruptcy  
4 analysis -- and I won't repeat any of the contract analysis  
5 that Mr. --

6 **MS. UNIDENTIFIED:** Santoro.

7 **MS. DAVIS:** I'm sorry, your Honor. It's been a long  
8 week. Mr. Santoro provided to the Court, but certainly we echo  
9 and agree with that analysis as it interprets the various loan  
10 documents that were signed by my client. Now, two of my  
11 clients are in the opaque loan and --

12 **THE COURT:** Now, it says that they're not going to  
13 accept the payoff and release until they verify that all  
14 amounts have been paid.

15 **MS. DAVIS:** Correct. And it would be helpful to know  
16 whether or not that has been done.

17 **THE COURT:** Okay.

18 **MS. DAVIS:** And second of all, your Honor, we need to  
19 look at this in the context of a cash collateral motion as  
20 well. We have collection of other people's money. The  
21 majority of this money is not property of the estate. The only  
22 portion of this money that's property of the estate is the  
23 servicing fee. The rest of it belongs to somebody else. So if  
24 you're going to take away their security interest, you have to  
25 give them something.

1           Now, I like Mr. Santoro's suggestion that we go ahead  
2 and open the separate bank accounts for the various different  
3 loans. I think they should do that for all of the loans.  
4 There are too many issues and too many unknowns about what  
5 happened in the past that we don't want to have repeated in the  
6 future.

7           I would also ask that under the Bankruptcy Code that  
8 each -- to the extent that your Honor authorizes the release of  
9 any security interest such as the security interest by my  
10 clients in the opaque loan, that they be granted a replacement  
11 lien in the funds that are placed in the separate account that  
12 Mr. Santoro has requested.

13           We have to look at this as a third-party lender being  
14 involved with a transaction that's in a bankruptcy case. We  
15 don't have property of the estate. Primarily, we have only a  
16 servicing fee, which is a very small amount of the  
17 \$5.8 million.

18           In conclusion, your Honor, I would like to re-  
19 emphasize that, you know, this is money that people are  
20 depending upon. My clients are only two of the investors in  
21 this loan. There are dozens of other investors in this loan.  
22 Many retired persons put their retirement money into these  
23 loans. We really have to come to grips with at some point  
24 making current payments to these people. And while it's  
25 laudable that, you know, Mr. Allison and the debtors need to

1 figure out what happened prepetition, in the meanwhile, post-  
2 petition something has got to happen for these other folks.

3 Thank you, your Honor.

4 **THE COURT:** Okay.

5 **MS. GUYMON:** Your Honor, if I may. Marjorie Guymon  
6 appearing on behalf of Roam Development Group. I was just  
7 recently retained and didn't want to face the wrath of the  
8 Court in filing a late responsive pleading.

9 My client doesn't necessarily object to the motion.  
10 But to bring in yet another perspective on this issue is the  
11 borrower's perspective in acknowledging that there are several  
12 named lenders in these documents, none of which are  
13 USA Capital, USA Mortgage. The borrower is concerned that in  
14 making the payment to the debtor that the lender is -- and then  
15 the lender not receiving the funds what is the lender going to  
16 do to the borrower.

17 **THE COURT:** Hang on a second. Ms. Chubb, you've  
18 got -- get us off speaker. We're hearing you rattle your  
19 papers.

20 **MS. CHUBB:** I'm not on the speaker. I'm sorry, your  
21 Honor.

22 **MS. GUYMON:** Unfortunately, I wasn't able to raise  
23 this in writing, and maybe it would be more appropriate to  
24 raise it in a separate motion. But specifically since my  
25 client is involved in this particular motion, Roam Development

1 Group, for example, the May payment was made into my trust  
2 account. It was timely made into that trust account. Similar  
3 to Fidelity, it would like a comfort order from the Court  
4 stating that by paying the debtor it is in compliance with the  
5 terms of the loan documents.

6 There is some concern that the borrower would not be  
7 in compliance with the terms of the loan documents to the  
8 extent that the lenders didn't receive the funds. And so based  
9 on that, if there could be some clarification or comfort order  
10 from the Court today as to what I do with those monies,  
11 certainly they need to be turned over to somebody and not sit  
12 in my non-interest bearing trust account. But that issue needs  
13 to be resolved.

14 **THE COURT:** Okay.

15 **MS. GUYMON:** Thank you.

16 **MR. McKNIGHT:** I agree with --

17 **MS. UNIDENTIFIED:** Can I get your name, again?

18 **MR. McKNIGHT:** Richard McKnight on behalf of the  
19 McKnight Family Trust.

20 Your Honor, it's not burdensome for them to go to a  
21 bank and open a separate account to put this money from Roam  
22 Development in. They have everyone -- all of the lenders'  
23 social security number so they can make their 1099 reporting at  
24 the end of the year. The bank is going to have a lot of typing  
25 to do to put all the names on the account. But then the money

1 could be put in that account and it's segregated and we know  
2 where it is and we know how much it is, and we don't have to  
3 put with things such as them reporting that Roam Development  
4 loan is a non-performing loan when it was two days late when  
5 they reported it. And now we find out from Ms. Guymon that the  
6 money is in her trust account for their May payment. So it's  
7 not non-performing at all.

8 And this would avoid that, because the bank could  
9 provide that information in some manner to all of the lenders  
10 so they'd be aware that these payments are being made even if  
11 we don't decide immediately to distribute. So I would  
12 heartedly agree with the separate account concept. Thank you.

13 **THE COURT:** Okay.

14 **MR. MEROLA:** Your Honor, on behalf of the investment  
15 committees, I don't know if I have a solution but I might have  
16 another problem.

17 What we're going to crash against in resolving this  
18 motion is the debtor's desire to hold all funds temporarily.  
19 That matter is not on calendar for today, but it's on for I  
20 believe June the 5th.

21 **THE COURT:** Uh-huh.

22 **MR. MEROLA:** I don't know how we resolve this motion  
23 without resolving or giving a preview on that other motion,  
24 which people haven't even filed replies and objections to.

25 **THE COURT:** And that occurred to me. But my thinking



1 was, as a practical matter, none of this money is going to be  
2 in the debtor's account until after June 5th. So I, quite  
3 frankly, kind of intended to deal with what do I do about the  
4 release aspect.

5 **MR. MEROLA:** Again, I just wanted to flag the issue.

6 **THE COURT:** Yeah.

7 **MR. MEROLA:** Because when we see the documents,  
8 obviously, that's something we're going to be talking about.

9 **THE COURT:** Exactly.

10 **MR. MEROLA:** On the 5th and everyone is going to have  
11 a lot to say about it at that time.

12 **THE COURT:** Exactly. Okay. Mr. Landis, you've been  
13 very patient.

14 **(Pause)**

15 Are you going to let the Code get in the way of  
16 things, Mr. Landis?

17 **MR. LANDIS:** No, I'm not, your Honor.

18 **(Laughter)**

19 I just like having my security blanket up here at the  
20 podium in case I get asked a good and hard question by the  
21 Court, and that's often likely.

22 The answer is this. I didn't have a dog in this  
23 fight at all until people started talking about separate  
24 accounts. We need to have limitations on the number of  
25 accounts that are maintained by the debtors in this case.

1 Because if we start opening bank accounts for every special  
2 interest in every single situation we're not only going to have  
3 a bazillion accounts, if you're concerned about administrative  
4 costs, it's going to get ungainly and unmanageable.

5 I think the appropriate way to address the concerns  
6 regarding identification and earmarking is through reporting by  
7 the debtor. We already have a debtor in possession account  
8 that is, in fact, receiving all of the money. The fact of the  
9 matter really is this: What the interested parties have  
10 requested is reasonable. We want to know that our money went  
11 into that account and that much of it is ours.

12 I think the obligation of the debtor was to have a  
13 debtor in possession account, and they do. And by reporting on  
14 an interim basis all of the parties in interest can have the  
15 information that they're seeking. We would simply request that  
16 to the extent that the Court decides to require additional  
17 information rather than a whole bunch of segregated accounts  
18 for every special interest the debtor just be directed to  
19 provide interim reporting in a meaningful way so that the  
20 parties can track their funds.

21 **THE COURT:** What is your thought about -- and, of  
22 course, the debtor's one of the biggest comment -- what's your  
23 thought about if I required separate accounts only on those  
24 loans for which we're providing releases?

25 **MR. LANDIS:** I don't know how many of those loans

1 ultimately will have releases in the near term, Judge.

2 **THE COURT:** Okay.

3 **MR. LANDIS:** And the answer is from a practical  
4 standpoint that might make some sense. I just can't address  
5 it, in particular, right now. I can certainly be in a position  
6 to do that come June.

7 **THE COURT:** I forgot to ask you. How are we dealing  
8 with the bond problem since this is over 100,000? Have you got  
9 that all dealt with? I mean not that there's any problem, but  
10 I mean it's a technical -- speaking of the Code, it's in the  
11 Code.

12 **MR. LANDIS:** Internally and through our program, yes,  
13 your Honor.

14 **THE COURT:** Okay.

15 **MR. LANDIS:** We're satisfied that that's being  
16 addressed right now.

17 **THE COURT:** Okay. Good, then. All right. Any other  
18 comments?

19 **MS. UNIDENTIFIED:** I'm sorry, your name again?

20 **MR. CONNAGHAN:** Paul Connaghan on behalf of the seven  
21 borrowers that I named earlier. And I just wanted to comment  
22 that we do not object and we join in the motion to the extent  
23 that we would ask for reconveyances to be executed, whether  
24 partial or full.

25 And also, it appears to me that Paragraphs 4 and 5 of

1 the servicing agreement pretty well spell out a means and a  
2 method for how much money should be paid for the services for  
3 collections for legal fees, and it's 3 percent. I show the  
4 same concern as Ms. Guymon. Money should be paid accurately  
5 and correctly to the investors in accordance with this  
6 agreement. I guess that's going to be addressed in a later  
7 hearing. I just wanted to --

8 **THE COURT:** How was it paid in the past? In your  
9 past experience, was it paid if it was a release or did your  
10 client not have releases in the past, your clients?

11 **MR. CONNAGHAN:** My client has seven loans. I'm not  
12 extremely familiar with them. I just --

13 **THE COURT:** Sure.

14 **MR. CONNAGHAN:** We were just retained yesterday. But  
15 monies were paid to the servicer and then, of course, the  
16 disbursements were made for interest if everything was done  
17 according to the agreements to the investors.

18 **THE COURT:** And I assume you would object to having  
19 to pay 100 separate checks on a \$90,000 --

20 **MR. CONNAGHAN:** Yeah. I think it should continue in  
21 the same manner and fashion as in the servicing agreements, and  
22 I don't believe it should be broken up. Beyond that I don't  
23 believe that it's proper to take their money and commingle it  
24 necessarily. The investor trust account what that was for  
25 certainly was to make sure that the investors' monies were

1 properly accounted for. But I don't think anybody here is  
2 arguing that the monies won't be accounted for and distributed  
3 for each loan and divided up accordingly.

4 **THE COURT:** Okay. Reply?

5 **MS. JARVIS:** Your Honor, let me first respond kind of  
6 generally and then I'll walk through the specifics.

7 I think if it's not clear to these objectors I think  
8 it should be made clear that we are not asking to continue past  
9 bad act practices. That is not what is at issue here. We are  
10 not -- Mr. Allison is coming here new. He is very careful to  
11 make sure that everything is done through -- you know, through  
12 the court. We have already indicated that all monies will be  
13 held in the collection account. Nobody's principal is going to  
14 be -- or interest in the loans are going to be released with no  
15 principal that is taken in or no added value that comes from  
16 the release of senior liens, which is contemplated by this. So  
17 we are not talking about the past practices where the debtor  
18 could use the money in any way or maybe did use the money in  
19 any way we wanted. It goes into a separate account and this --

20 **THE COURT:** So, you know, the 90,000 comes in on one  
21 condo you just sold.

22 **MS. JARVIS:** Right.

23 **THE COURT:** What is the accounting entry? Is it  
24 shown that, for example, Ms. Davis's client gets \$16.25?

25 **MS. JARVIS:** It's accounted for by loan. And then

1 what we're -- what Messer (phonetic) was working on now is to  
2 then account for by investor. That's what we're talking about  
3 by June 15th. Right now when it comes in I believe it's  
4 accounted for by loan. So we can show that this much came in,  
5 it belongs to this particular loan.

6 And this is a procedure, your Honor, that we already  
7 addressed and got approval for in the cash management motion  
8 where instead of having 115 separate accounts we have one  
9 account that there are 115 separate accountings that gone on so  
10 when the money comes in, you know, it is identified and traced  
11 with respect to the particular loan.

12 **THE COURT:** So we would know if that money came in  
13 tomorrow we would be able to ascertain exactly how much a  
14 particular investor would be entitled to on account of that  
15 release.

16 **MS. JARVIS:** Right, right. Not on account of what  
17 other, you know, investment --

18 **THE COURT:** Right. Just on account of that release.

19 **MS. JARVIS:** -- and loans, but on that account and  
20 release. And, in fact, your Honor, the committee raised the  
21 issue of whether we could report that on a monthly basis. Yes,  
22 we can -- we are willing to and we can account for releases and  
23 we'll file that along with our monthly reports so parties can  
24 see that. Now, hopefully, you know, we'll be able to get to a  
25 point where we can begin releasing money, you know, to

1 investors so this doesn't become such an issue. But in the  
2 interim, that is what we intend to do.

3 **THE COURT:** Now, going back to the issue concerning  
4 defaults. Another side of that coin is to what extent when  
5 you're providing releases is the -- Mr. Allison confident  
6 enough that there are no other defenses to the loan? For  
7 example, if the loan was received with the breached warranty, a  
8 material warranty such as let's assume -- worst case basis,  
9 they submitted an appraisal they knew was false. You would  
10 have then a defense -- you could call a default and you'd also  
11 have a defense to the release, the request for a release.

12 To what extent are we at the stage that you're  
13 confident that -- you can never be 100 percent confident -- but  
14 that the loan was made in accordance with the representations  
15 of the lender or the borrower?

16 **MS. JARVIS:** Well, one of the things that we have on  
17 for hearing on June 5th is the retention of Hilco to do  
18 appraisals. And they actually have already started to do that.  
19 I think they're about 50, you know, percent through because  
20 they were willing to go ahead and do it with the application on  
21 file. That is one protection because he then has independent  
22 information with respect to the value of this property and kind  
23 of where -- you know, where the loan stands with respect to the  
24 value of the property.

25 And not in -- in all cases it isn't necessarily money

1 that's being released because sometimes it's paid off. In some  
2 cases there is a senior lienholder, and so the money is paid  
3 off on the senior lienholder, which then instead of money  
4 going, you know, to the lenders --

5 **THE COURT:** Right.

6 **MS. JARVIS:** -- they're actually increasing their  
7 value in the property. But there is that protection that is  
8 under way and in place. And there have been a substantial  
9 amount of work done in reviewing each loan file in order to,  
10 you know, try to identify, you know, as many issues as we can  
11 with respect to dealing with these loans.

12 **THE COURT:** I mean, you know, if you release a  
13 portion of the collateral, obviously, you're not waiving your  
14 defenses.

15 **MS. JARVIS:** Right.

16 **THE COURT:** But the point is you then have arguably  
17 less collateral from which to realize --

18 **MS. JARVIS:** Right. And that's why it's important to  
19 get, you know, independent appraisal information so we really  
20 have an idea about, you know, the current value of the  
21 collateral, whether there are any issues with respect to that.  
22 And that is under way and he is working on that with respect to  
23 moving forward.

24 **THE COURT:** Okay.

25 **MS. JARVIS:** Let me address the specifics as well.



1 Let me understand. When I raise kind of the pragmatic side,  
2 I'm not saying that isn't what the documents say. Because the  
3 documents are in accord with that. I mean what was read to you  
4 is just kind of parsing through certain things. And I think in  
5 our reply brief we carefully walked through that with the  
6 Court. Because the loan servicing agreement in Paragraph 2  
7 does allow us to collect principal as well as interest and to  
8 take whatever actions we need to do to collect that.

9 Now, while in the provision that the -- Paragraph 11  
10 of the loan servicing agreement, which was cited to you, the  
11 sense just that nobody has to look beyond the declaration of  
12 the agency, that actually comes after a description of the  
13 powers that Commercial Mortgage has as the loan servicer, which  
14 would include giving these releases and doesn't diminish that.  
15 In fact, what that says is as between third parties they can  
16 look at this power of attorney, but it doesn't change the  
17 rights between the loan servicer and the lenders, which is the  
18 right to collect these funds and grant releases, which includes  
19 collection of principal.

20 In addition, as we have argued, in Paragraph 2 of the  
21 loan servicing agreement when it talks about collecting this,  
22 it talks about paying the proper parties; and again, that's  
23 where we get to the point why we have on file the motion to  
24 hold funds, which is not before the Court at this time. But  
25 that is an issue as to why these funds needs to be collected in

1 the way they normally were collected because we can't assure  
2 without these total accountings that the proper parties are  
3 paid. Because some people, you know, weren't paid when they  
4 were supposed to. And there are these various issues. So it  
5 is consistent with the loan servicing agreement.

6 In addition, when you look at the power of attorney,  
7 the provision that was cited to you also says "in accordance  
8 with the deed of trust." And the deed of trust that was shown  
9 you talks about being paid to the lender. But if you go down  
10 the page, it shows you that the lender is identified and the  
11 payment is directed to USA Commercial Mortgage. And that's the  
12 address that it is sent to. So this is -- what we're asking  
13 for is in accordance with the documents. And the fact that the  
14 past practices were like that is simply evidence that that is  
15 consistent with what the documents say and how it should be  
16 accomplished.

17 Now, obviously, you know, we're in the -- you know,  
18 we're trying to collect all we can on these loans. And as we  
19 move forward it is -- Mr. Allison is working towards and  
20 intends to try to get money out to investors as soon as  
21 practical in making sure that everybody gets what they're  
22 really entitled to given the difficulties that have arisen from  
23 the past practices in this case.

24 And it is important that these documents be complied  
25 with, that these practices that are consistent with these

1 documents be adhered to so that money can be collected in the  
2 ordinary course and these issues with respect to investors can  
3 be sorted out and the proper parties paid.

4           So we do believe that we have shown your Honor  
5 through walking through this, this is consistent with the  
6 documents. It's also consistent with the past practice, which  
7 I think evidences that is a valid reading of the documents.  
8 And it is consistent with what needs to be done for the  
9 interest of all of the creditors in this estate as well as the  
10 pragmatic, you know, results.

11           **THE COURT:** Okay. All right. I'm going to allow the  
12 releases. I'm going to authorize Mr. Allison to make releases  
13 on loans that are not in default and in accordance with the  
14 terms of the notes and deed of trust and to the extent that  
15 there does not appear to be a significant defense to the note  
16 and deed of trust -- to the release.

17           Now, that may put him more in a quandary, but I think  
18 certainly, you know, you can accommodate that like we do on  
19 secured lender situations. You know, you ask them for  
20 warranties that, yes, indeed, it was not in default; yes,  
21 indeed, all representations were true. Perhaps you can even  
22 ask for a warranty that, you know, they warranted that all  
23 representations are true and they acknowledge that those  
24 representations were not true; that, you know, there's no  
25 waiver. I mean you release that particular property.

1           And again, we're talking about third parties buying  
2 these condos, so we don't them subject to the deed of trust. I  
3 assume you still have a deed of trust on the common areas and  
4 all these properties, in any case.

5           **MS. JARVIS:** I believe that's true.

6           **THE COURT:** Now, I will not deal with it today, but  
7 as a practical matter, no monies will be coming in before  
8 June 5th. I don't think; will there be?

9           **MS. UNIDENTIFIED:** They might.

10          **THE COURT:** Okay.

11          **MS. DAVIS:** Your Honor, the opaque money was received  
12 at the end of April.

13          **THE COURT:** Okay. I will hold ruling who gets those  
14 monies until June 5th. I want you -- and I have not focused  
15 that motion -- but I want you to specifically address at that  
16 hearing the comments raised by Mr. Walch and Mr. Santoro. And  
17 I want to specifically understand whether or not we should make  
18 distinctions with a going forward basis, with releases, whether  
19 there are any loans in defaults, and with the specific point  
20 that he pointed out.

21               I mean you addressed this as far as what the deed of  
22 trust requires, but I need a little more focus on, you know, if  
23 there's a release is it, indeed, required to be paid to them  
24 immediately. I think it's all right that it be paid to USA  
25 Commercial now; that's the only thing that makes sense. It may

1 make sense, too, to do it a practical diminimis thing; in other  
2 words, the monies comes in, they're paid if the checks amount  
3 to \$200 total. I mean, you know, to write \$12.50 checks to  
4 everybody. You know, for example, 95,000 and 25 million is a  
5 pretty small percentage. And then once you divide that up,  
6 that's, you know -- eats more administrative time.

7           While, on one hand, the idea of separate bank  
8 accounts is appealing, the U.S. Trustee's comment is well  
9 taken; and, of course, we've sort of addressed that before.  
10 But it may be appropriate as this case goes along to set up  
11 separate accounts in some of these situations. You know, if  
12 you've got a lot of partial releases coming in, it may make  
13 some sense. But I think we can address that in the context of  
14 what happens to the money once it comes in. The June 5th  
15 hearing will be very important in that regard.

16           **MS. JARVIS:** So, your Honor, just to make sure I  
17 understand. You can go ahead and do these releases with these  
18 conditions. And, of course, Mr. Allison is a former banker so  
19 he's fully aware of the types of protections he needs to take  
20 with respect to getting these releases. The money that comes  
21 in between now and June 5th we can put in our collection  
22 account; we will separately account for it.

23           **THE COURT:** Of course, again --

24           **MS. JARVIS:** Yes.

25           **THE COURT:** -- that's relying on the representation

1 being separately accounted.

2 **MS. JARVIS:** Yes.

3 **THE COURT:** Et cetera.

4 **MS. JARVIS:** And then at the June 5th hearing you  
5 would like us to address the issue of whether, for instance,  
6 once a principal repayment is that a different issue, and an  
7 interest payment --

8 **THE COURT:** In other words, I'm reserving -- and this  
9 is the back half of your motion, the motions that have been  
10 raised, Mr. Santoro and Mr. Walch and Ms. Davis. I think  
11 they're better all dealt with in the context -- by that time  
12 we'll have a better sense, too, of is there a legal difference  
13 between, all right, you're entitled to payment; what rights do  
14 you have of offset; and are there rights of offset even  
15 assuming that some of these people have gotten more than they  
16 have. And those are issues you're just going to have to  
17 address in that context.

18 **MS. DAVIS:** Yes, your Honor. Will we get the  
19 replacement lien that we requested --

20 **THE COURT:** Oh, yes, I'm sorry. Excuse me. Yes.  
21 And, of course, all these monies will -- all the liens will  
22 attach to the monies in the bank account.

23 **MS. JARVIS:** That's correct. We're not --

24 **THE COURT:** I think it's -- yeah, it's obvious. But  
25 it's a good thing we need to say it's -- to make that obvious.

1           **MR. FLEMING:** Your Honor, I need to ask for --

2           **MS. UNIDENTIFIED:** Your name, please?

3           **MR. FLEMING:** Yeah. Scott Fleming on behalf of Bank  
4 of America.

5           Your Honor, the bank has a first priority deed of  
6 trust that encumbers two of the properties that were the  
7 subject of this motion. The first is the Parkridge Condominium  
8 project in San Diego. It's owned by 5252 Orange LLC. And the  
9 second is the Glenridge Condominium project owned by 60th  
10 Street Venture, LLC.

11           The bank is in a somewhat different situation here,  
12 because all proceeds from the sale of these units are first  
13 paid to the bank until its loan is satisfied in full, at which  
14 point all future payments will then be directed to the debtor  
15 or to whomever the lenders are ultimately held to be.

16           I understand you've authorized Mr. Allison to execute  
17 reconveyances post-petition. It has been the practice of the  
18 parties all the way back to the beginning of these loans to  
19 allow the bank to record the reconveyance on behalf of the  
20 debtor. What happened in this case --

21           **THE COURT:** This debtor?

22           **MR. FLEMING:** Yes.

23           **THE COURT:** USA Commercial?

24           **MR. FLEMING:** Yes. What had happened, your Honor,  
25 was because the bank was receiving all of the --

1           **THE COURT:** I mean Bank of America can release its  
2 deed of trust, but how in the world can it release  
3 USA Commercial?

4           **MR. FLEMING:** Well, when the loan was funded as a  
5 condition to granting the loan the bank required the debtor to  
6 provide reconveyances that were executed with the understanding  
7 that the bank would then, pursuant to a power of attorney,  
8 record those reconveyances as individual units were sold so  
9 these things could get closed very quickly and easily.

10          **MS. JARVIS:** As long as the conditions were met.

11          **MR. FLEMING:** Of course, yes. And, in fact, that  
12 system has worked beautifully, your Honor. We have on the  
13 5252 Orange property the original principal amount of the loan  
14 was \$16 million. And as of today that's been reduced down to  
15 about 2.2 million. So the procedure that we've been --

16          **THE COURT:** Well, but that's your loan. How much is  
17 the USA -- the debtor's loan?

18          **MR. FLEMING:** My understanding is that loan has a  
19 balance of about 3.8 million.

20          **THE COURT:** So how much is the property that's not  
21 released still worth?

22          **MR. FLEMING:** I have numbers as of --

23          **THE COURT:** Isn't that a bigger question?

24          **MR. FLEMING:** Sure, your Honor. We understand  
25 there's plenty of equity in both these properties. I have



1 numbers that are good as of April 26th. We understood that as  
2 of that date with respect to the 5252 Orange property, 51 of  
3 the 104 units have been sold. Again, as of April 26th of 2006,  
4 that the balance of the bank's loan had been reduced to about  
5 3.6 million. And because of the -- even in the three weeks  
6 since then it's gone down to 2.2.

7 **THE COURT:** Well, I don't understand how the bank  
8 would have the power to re-convey the debtor's deed of trust  
9 especially without -- you know, if that was an executory  
10 contract it's -- I don't understand that at all.

11 Mr. Merola had a comment?

12 **MR. MEROLA:** Yeah. That is absolutely terrifying,  
13 your Honor. Frank Merola on behalf of the investor committees.

14 To the extent there were prepetition executed  
15 reconveyances delivered and delivered either pursuant to a  
16 power of attorney that are now being recorded releasing liens  
17 by the debtor or the direct investors, that can't happen.  
18 That's in violation of the automatic stay. It's without  
19 authority of the debtor in possession. The only person  
20 authorized to issue reconveyances on behalf of this debtor in  
21 possession should be Mr. Allison. And if there are documents  
22 out there from the old insiders giving people reconveyance  
23 rights that we don't control, that can't happen. And we would  
24 take the position that any of those reconveyances are in  
25 violation of the stay and void, per se.

1           **MS. JARVIS:** Let me just step in and explain. We're  
2 not asking to allow them to just record, you know, liens  
3 whenever they feel like it. You would still have to go through  
4 the same process where Mr. Allison would say: Yes, you know,  
5 you're authorized; go ahead and release this.

6           And the question for I think us is simply do we allow  
7 them to continue to use these partial releases that they hold,  
8 or do we have to go through the process of --

9           **THE COURT:** I don't see how.

10          **MS. JARVIS:** -- executing new ones.

11          **THE COURT:** I mean I don't see -- he's absolutely  
12 right. If the bank purported to do it, they're void to the  
13 extent they're issued prepetition and not recorded.

14          **MS. JARVIS:** Right. Well right and --

15          **THE COURT:** I mean to the extent they're not recorded  
16 prepetition.

17          **MS. JARVIS:** And all I was raising is as a -- I think  
18 for us it's more just a technical issue, you know. It has to  
19 be authorized by Mr. Allison. The question is just can he do  
20 it through saying: Okay, go ahead, record these. Or does he  
21 need to --

22          **THE COURT:** I say no, do it himself.

23          **MS. JARVIS:** -- execute a new one.

24          **THE COURT:** I mean that's just --

25          **MS. JARVIS:** Okay. Okay. We'll do a new one.

1           **THE COURT:** Who knows what the agreement is? Who  
2 knows what the indemnity rights are? That's just one more  
3 problem we don't need. We've got enough in this case.

4           **MR. FLEMING:** Okay. Thank you, your Honor.

5           **THE COURT:** One more comment?

6           **MR. MASON:** Judge, once again Richard J. Mason on  
7 behalf of Dr. Kantor and related interests.

8           Judge, I would hope that the order which you enter  
9 will provide that rights of setoff and recoupment will not be  
10 affected, impaired, modified in any way by virtue of the fact  
11 that the debtor is going to be taking the money into the debtor  
12 in possession account.

13           **THE COURT:** Right. I think that's a good point. So,  
14 in other words -- and that's kind of a reason I want to wait  
15 until June 5 --

16           **MR. MASON:** Yes.

17           **THE COURT:** -- to suggest, and that's a good point to  
18 actually say that as well. But whatever rights parties had --  
19 someone is calling it a Popeye (phonetic) order. Whatever it  
20 is, it is. So everybody's rights are preserved with the money  
21 coming into the account.

22           **MR. MASON:** Thank you, Judge.

23           **THE COURT:** Okay.

24           **MS. JARVIS:** And, your Honor, I think that actually  
25 was stated in our cash management motion --

1           **THE COURT:** Okay, good.

2           **MS. JARVIS:** -- that as we collected -- all rights  
3 are preserved in, you know, all the monies that we collect.

4           **THE COURT:** Okay, good. All right. Let's take one  
5 more recess and then we'll go to the DIP financing.

6           **THE CLERK:** All rise.

7           **(Recess taken from 12:22 p.m. to 12:32 p.m. / Parties**  
8 **present)**

9           **THE CLERK:** Court is now in session.

10          **THE COURT:** Be seated. Okay, to the due diligence  
11 phase, let me -- I guess we need to wait for everybody to get  
12 in. I guess we've got all Counsel here.

13           Let me tell you what my thoughts are in the beginning  
14 of this case. We're all sick of each other. So let me just  
15 cut a little bit to the chase. Let me tell you. I have some  
16 real problems with this due diligence and I'll certainly hear  
17 from the proponents as well as the opponents. My problem is  
18 the amount of the fee. First of all, it's not just a hundred  
19 and fifty thousand. It's a hundred and fifty thousand plus the  
20 other costs. It's just a hundred and fifty thousand up front.  
21 I'm really not so sure that -- I want to say Force. That's not  
22 it.

23          **MS. UNIDENTIFIED:** Fortress.

24          **MR. UNIDENTIFIED:** Fortress.

25          **THE COURT:** Fortress -- who by the way bought the

1 Michael Jackson loan from B of A -- really would not do it if  
2 they didn't get their due diligence fee. Secondly, they've  
3 already done their due diligence. So I'm not so sure it's  
4 necessary now to be in a position later to decide what we're  
5 going to do. The more important concern I have is the slippery  
6 slope aspect of this which is interrelated with the cost. I  
7 just don't think this estate can afford to ship out a hundred  
8 and fifty grand right now when we're in such a crucial stage of  
9 trying to figure out what is going on.

10 Secondly, I have my doubts about whether or not this  
11 case really needs DIP financing. Now, on one hand to the  
12 extent you need financing to collect on loans, you told me just  
13 two weeks ago that you had enough money to administer this case  
14 at least for 90 days and you said you've got enough money from  
15 servicing to administer the case. To the extent that you want  
16 to make the new loans, it's certainly premature because we  
17 don't know what's going to happen. It may make more sense for  
18 the Debtor to sell its rights to make the loans to somebody  
19 else and certainly in any case -- I know the loan is not before  
20 me today but it becomes a real slippery slope.

21 I would want to see how in the world it would pencil  
22 up. I can't vision how in the world it will pencil out to pay  
23 a hundred and fifty thousand plus the rest of the fees and  
24 that's just peanuts in this stage and then pay a million --  
25 let's see -- 2.5 million for commitment fees. Of course, it

1 comes out of what they're going to give you but you're paying  
2 interest on the whole thing and the interest is at 10 plus  
3 LIBOR. I don't see how in the world it would ever pencil out,  
4 especially in today's market going down. That's something you  
5 could show me later but my problem is if I authorize a hundred  
6 and fifty thousand now, I'm on that slippery slope and now when  
7 it comes time to authorize the loan, I'm -- well, your Honor,  
8 we spent a hundred and fifty thousand dollars. We've got to go  
9 forward.

10 So again -- and since the commitment is already here,  
11 I appreciate the fact that the potential lender was ready to  
12 show you what they're willing to do but by the same token, I  
13 know that they really have done their due diligence already.  
14 So -- for the most part. So this is my thinking. I am  
15 basically not willing to authorize the payment of a due  
16 diligence fee at least at this stage until we know more about  
17 the case. Go ahead.

18 **MS. JARVIS:** Let me just address first a little bit  
19 why we're coming at this stage of the case. There are three  
20 reasons --

21 **THE COURT:** And I'm sorry. I need one more very  
22 important factor and I apologize. I am unclear -- again this  
23 slippery slope aspect -- how in the world we would ascertain  
24 what collateral they're getting. That seems to me to encompass  
25 more fights than later. I mean, let's assume we say, okay,

1 fine, you've got a collateral -- you've got a security interest  
2 on the Debtor's collateral. Well, now we have -- when we have  
3 our later fights about inter se, who has the rights to the  
4 collateral, we've now got a big pocket, a deep pocket in that  
5 dog fight and I just don't know if these investors should be  
6 subjected to one more dog in the fight. Sorry, go ahead.

7 **MS. JARVIS:** There are three reasons why we've gone  
8 forward to try to get DIP financing initially or right off the  
9 bat and the first is dealing with the operational expenses.  
10 Now, while your Honor points out correctly that we have enough  
11 for 90 days, you may recall that after that 90-day period, the  
12 reason why we've re-noticed this up is because unless we get  
13 loan origination fees or we have some other funding, then we  
14 don't necessarily have enough funds to continue and so in  
15 looking ahead towards that -- and the reason why is clear.  
16 It's because we have a loan portfolio we're servicing that is  
17 60 percent nonperforming. In fact, I think it may be 72  
18 percent. Anyway, it's -- no, it's 60 percent.

19 So when you have that many nonperforming loans, your  
20 cash flow is strapped and basically what the DIP financing does  
21 is fills that gap. It allows money to come in so you then can  
22 use it to make these loans to become performing and then pay  
23 back the DIP financing. So it allows us to go forward to turn  
24 the nonperforming into performing loans and then money cash-  
25 flows in, of course, on a better basis and of course the

1 interests of the investors are preserved by allowing for money  
2 to make sure that these loans can be properly enforced and  
3 collected.

4           The second reason -- and that -- there is that 90-day  
5 window and so when we're looking out -- well, the reason why  
6 we're starting now is because we want to make sure that there's  
7 plenty of notice given when we actually get the terms so that  
8 people can, you know, argue about it. We can deal with the  
9 collateral issues in discussions with parties so that by the  
10 time we get to that, the end of that 90-day period, all of  
11 those things have been worked out. It's been properly noticed  
12 and we can hopefully go forward, you know, at that point in  
13 time.

14           If we delay, then we get into a situation where it's  
15 too late. So we're looking ahead towards making sure the  
16 process works in giving everybody adequate notice and an  
17 opportunity to be heard on this.

18           **THE COURT:** Well, how much cash is there in the  
19 servicing account now? We're talking the servicing-only  
20 account. We're not talking money in the investor accounts --  
21 servicing only.

22           **MS. JARVIS:** You mean the money we've transferred so  
23 far in accordance with our budget, you know, that is currently  
24 held --

25           **THE COURT:** Well, what's legitimately yours under a



1 servicing agreement.

2 **MR. UNIDENTIFIED:** It's not that much. It's three or  
3 four digits between 3 and \$400,000 is --

4 **MS. JARVIS:** About 3 to \$400,000.

5 **THE COURT:** So you're going to pay -- and on 3 or  
6 400,000, you're going to pay this lender a hundred and fifty  
7 thousand now. How are you going to operate in the next month?

8 **MS. JARVIS:** Well, let me -- well, of course there'll  
9 be more monies coming in in the next month. This is what we  
10 currently have and let me just address, you know, two issues  
11 with that being -- with respect to that. The first is that  
12 hundred and fifty thousand -- one of the things we bargained  
13 for when we did this is their due diligence that they do is  
14 turned over to us. So to the extent they do appraisals with  
15 it, we get those appraisals. To the extent they've done, you  
16 know, a review of the loans and, you know -- then all of that  
17 information becomes our information. So --

18 **THE COURT:** But you don't know what that is at this  
19 stage.

20 **MS. JARVIS:** Yeah, but we're trying to accomplish the  
21 same thing. In other words, what happens is that basically  
22 this helps us move the process along faster because we now get  
23 -- you know, as they're going through and doing this, they're  
24 going to turn it over to us.

25 **THE COURT:** We know Counsel charges three times what

1 you're charging. I mean, I'm serious. He probably charges  
2 \$600 an hour. So it's two times, two to three times.

3 **MS. JARVIS:** And it's useful for us not -- but it's  
4 useful for us not only in working out, you know, our own  
5 internal review of the loans but also to the extent that we  
6 can't work out this financing and we need to go forward with  
7 somebody else, it is useable for us in that vein too. So it's  
8 something we actually are getting some value for, you know,  
9 immediately.

10 The second problem that we have is these unfunded  
11 requirements and we've got 67 million of those and the -- part  
12 of this due diligence would go through and do due diligence on  
13 those. We've prioritized those. There's some that are very  
14 critical because they're projects maybe that are partially  
15 done. You've got a construction project. If you don't get  
16 funding, then you've Mechanic's Liens, potentially a shut-down  
17 of the project, a loss of value or in some cases, it's an  
18 amalgamation of land in order to make it, you know, more  
19 valuable for those currently in those loans and all of those  
20 decisions will be made. This is also why we've gone forward to  
21 hire Hilco because they would be made on a commercially  
22 reasonable basis.

23 **THE COURT:** Well, why couldn't you -- I mean, just  
24 like in every project -- let's assume this is a construction  
25 project. Let's assume that this was a construction company.

1 What you'd do is you would look at each loan and see whether or  
2 not that particular loan needed financing and you'd get a  
3 borrower like a simple Bank of America or a simple Wells Fargo  
4 as opposed to this fund that's charging these outrageous fees.  
5 I mean, they make their money by charging these outrageous  
6 fees.

7 **MS. JARVIS:** Well, I think, your Honor, that with  
8 respect to the unfunded commitments, I mean, what we would get  
9 for that is what we believe would be a commercially reasonable  
10 loan on that given the types of projects we've got and these  
11 are not the --

12 **THE COURT:** Ten plus LIBOR?

13 **MS. JARVIS:** Well, these are, you know, risky -- I  
14 mean, there's a reason why these loans --

15 **THE COURT:** Why do we think that you wouldn't get a  
16 loan from somebody else on a particular project? If the  
17 project -- and then second, if you're paying ten plus LIBOR,  
18 how in the world do you make the spread?

19 **MS. JARVIS:** Well, your Honor --

20 **THE COURT:** How in the world would you possibly --

21 **MS. JARVIS:** -- well, your Honor, we wouldn't -- I  
22 mean, this wouldn't be done unless there is value in the  
23 property that we'd be able to cover that. I mean, it's going  
24 to be a commercially reasonable decision.

25 **THE COURT:** Well, if there's value in the property,

1 then you can get the money from Wells Fargo at about half the  
2 price -- a Wells Fargo, a Bank of America, a Wachovia.

3 **MS. JARVIS:** Your Honor, it might be helpful to --

4 **THE COURT:** Okay.

5 **MS. JARVIS:** -- have Mr. Allison come up and, kind  
6 of, discuss this or put him on the stand because I think, you  
7 know, he's looked through this. He's made a decision and I  
8 think maybe he can express better than I can, you know, the  
9 reason why we need to go forward on the issues.

10 **THE COURT:** Well, I'm -- you know, I'm just skeptical  
11 about -- it's too early to decide if we're going to go forward  
12 or not. I'm just skeptical why we would need a due diligence  
13 fee at this stage and I don't want to get caught in a slippery  
14 slope and I --

15 **MS. JARVIS:** And I -- I can tell your Honor that  
16 there hasn't been any legal due diligence done by Fortress.  
17 They've done, you know, on-the-ground due diligence but not  
18 legal due diligence because they've held off until they -- as a  
19 requirement to get this fee to cover part of their costs and  
20 let me clarify. We're not asking for the, you know, hundred  
21 and fifty thousand plus more at this point in time. All we're  
22 asking for is the hundred and fifty thousand. With respect to  
23 anything --

24 **THE COURT:** But then they're entitled to it. The  
25 agreement says once they're -- once you hire them for due

1 diligence, they're entitled to the whole thing.

2 **MS. JARVIS:** But we sought approval only for the  
3 hundred and fifty thousand at this point in time.

4 **THE COURT:** What difference does it make? If you've  
5 now entered into a contract, you've got administrative expense  
6 for -- let's assume he spends 300,000 -- of course it has to be  
7 subject to reasonableness but let's assume I see you reasonably  
8 spent the time going through each loan document.

9 **MS. JARVIS:** But that would be part of the approval,  
10 you know, the loan, the cost of the loan.

11 **THE COURT:** The agreement says that he's entitled to  
12 due diligence, not only the hundred and fifty but the amounts  
13 they also spend subject only reasonableness even if they decide  
14 not to lend.

15 **MS. JARVIS:** But today we're asking for the hundred  
16 and fifty thousand and if we're asking for more --

17 **THE COURT:** But aren't you asking me to approve the  
18 agreement?

19 **MS. JARVIS:** No, we're not asking to approve the  
20 agreement. We're asking to approve the due diligence fee so we  
21 can go forward and ask for approval of the agreement. What we  
22 intend on doing is if the Court grants this today, we will file  
23 a motion on Monday.

24 **THE COURT:** Oh, well, I realize that. Now to put a  
25 term sheet -- well, wait a minute. If he's ready to do a term

1 sheet, they've obviously done their due diligence, right?

2           **MS. JARVIS:** They've done partial -- well, but they  
3 could have been subject to further due diligence and to the  
4 payment of this due diligence fee. So they've done an act of  
5 due diligence to give us a commitment with conditions but part  
6 of those conditions are they are finishing off the due  
7 diligence and in particular the legal due diligence and the  
8 payment of the due diligence fee.

9           **THE COURT:** Okay. All right.

10           **MS. JARVIS:** And -- so -- I mean, the problem we've  
11 got here is the timing is critical and we need to move forward  
12 in not only making sure that we don't have any shortfalls and  
13 be able to manage the -- you know, the nonperforming loans in  
14 this portfolio but also in order to start working through these  
15 unfunded commitments because some of them are critical.  
16 They're coming up right away and we need to be able to deal  
17 with those and like I said, each decision will be made on, you  
18 know, a commercially reasonable basis looking at does this make  
19 sense for the lenders that are currently in there to preserve  
20 their value.

21           This is not -- those unfunded requirements are not  
22 going to be done just to be originating new loans. They're  
23 going to be done in order to preserve the value of loans that  
24 are currently being serviced by Commercial Mortgage but they're  
25 coming up soon --

1           **THE COURT:** Okay.

2           **MS. JARVIS:** -- and to wait on this, you know, puts  
3 us in a difficult position. There is also a third part of this  
4 is not part of this --

5           **THE COURT:** Well, I guess I also wonder, you know --  
6 and this is a better question to ask Counsel for the purported  
7 lender. You know, why should we pay for them to decide if they  
8 want to make the business decision to make a loan? Now, I  
9 understand that, you know, this is usually done in these big  
10 cases but it's because nobody said "No." I mean, if I go out  
11 and I want to buy a house, I don't expect the seller to pay me  
12 for looking as whether or not I want to buy their house and how  
13 this came about in bankruptcies as being something as ordinary  
14 course of business is just strange to me.

15           **MS. JARVIS:** And this is part of the reason why we  
16 took a twist on this and bargained for, you know, getting this  
17 due diligence because in the example of the house, if you're  
18 paying for them to inspect the house and they turn over the  
19 results of the inspection, then there is some benefit to that.  
20 So we haven't -- we aren't just paying this and getting nothing  
21 for it. We have bargained, you know, for something that's  
22 different than what you see in normal cases and that is that we  
23 get the results of their due diligence, if they do appraisals,  
24 if they do --

25           **THE COURT:** Well, but you're going to go ahead and do

1 your own appraisals. Does that mean that you're going to ask  
2 that no appraisals be done until they do theirs first?

3 **MS. JARVIS:** No, they will coordinate with them  
4 because we're in the process of prioritizing -- doing  
5 appraisals and obviously, you know, we've already said that  
6 with respect to, you know, we're looking at appraisals that are  
7 in our files. You know, we're carefully reviewing exactly what  
8 we need and that would be something that we would coordinate  
9 with them as well.

10 **THE COURT:** Okay. All right, any other comments?  
11 I'm sorry. I have to ask your name again.

12 **MR. SAMUELS:** Joel Samuels of Sidley Austin for  
13 Fortress. I just want to correct some misperceptions your  
14 Honor may have based on your initial comments. We had asked --  
15 and, in fact, the term sheet contemplates that the Debtor ask  
16 your Honor to approve the term sheet in toto and --

17 **THE COURT:** Well, I understood the term sheet is not  
18 before me today.

19 **MR. SAMUELS:** Correct. And it's only the hundred  
20 fifty thousand that is before you at this time.

21 **THE COURT:** But you don't disagree that if I approve  
22 that, then we're committed -- the estate is committed to paying  
23 you 300,000 if I find that amount is reasonable.

24 **MR. SAMUELS:** Judge, if you found out that was  
25 reasonable, that's right.



1           **THE COURT:** Okay.

2           **MR. SAMUELS:** If you found that was -- and if I keep  
3 having to come back to these hearings over and over again,  
4 the --

5           **THE COURT:** Well, that's the thing. You've been here  
6 twice and you're going to charge that against the estate and I  
7 don't know why it was reasonable that you came the last time  
8 but you came.

9           **MR. SAMUELS:** Judge, because that was part of the  
10 initial due diligence it was, frankly, the only legal due  
11 diligence that we've been authorized to do.

12           **THE COURT:** Why couldn't you get a transcript?

13           **MR. SAMUELS:** Pardon me?

14           **THE COURT:** Why couldn't you get a transcript?

15           **MR. SAMUELS:** I possibly could have gotten the  
16 transcript. I possibly could have gotten the transcript.

17           **THE COURT:** How much did you charge for the trip over  
18 here?

19           **MR. SAMUELS:** I wrote down eight hours of time.

20           **THE COURT:** And that's how much?

21           **MR. SAMUELS:** Probably 4 to \$5,000.

22           **THE COURT:** Transcripts are a hundred and fifty  
23 probably.

24           **MR. SAMUELS:** I understand that, Judge, but there is  
25 something about knowing the people involved in the case and

1 getting a feeling of the case and being in the courtroom.

2 There just is.

3           The notion of a due diligence fee is -- has become a  
4 standard provision and I'm not going to get into whether it  
5 ought to have been but this is not an unusual thing to have a  
6 due diligence fee for a DIP financing transaction, number one.  
7 Number two, with respect to -- your Honor referred to LIBOR  
8 plus ten. The actual interest rate on the DIP loan, the 25  
9 million-dollar DIP loan is LIBOR plus 350. That's on Page 3 of  
10 the term sheet. I think your Honor was probably looking at  
11 Page 4 of the term sheet which is with respect to the so-called  
12 additional DIP loans which aren't even agreed to in any way.  
13 These are if we agree to it, the rate depending on our --

14           **THE COURT:** No. What's the effective interest rate  
15 though on the fact that you're not lending 25 million? You're  
16 only going to lend 22 million, whatever.

17           **MR. SAMUELS:** Well --

18           **THE COURT:** What's the effective rate --

19           **MR. SAMUELS:** -- I can go through all the fees,  
20 Judge.

21           **THE COURT:** Wouldn't the effective rate be a lot  
22 more?

23           **MR. SAMUELS:** The effective rate when you advance  
24 less obviously goes up a little bit more but this is not. I've  
25 seen --

1           **THE COURT:** Not just a little, right?

2           **MR. SAMUELS:** Well, it depends on how much and you've  
3 got to do the math but the origination fee, Judge, is one and a  
4 half percent of the maximum committed amount and, again, this  
5 is not before your Honor right now.

6           **THE COURT:** I understand.

7           **MR. SAMUELS:** You seem to be worried about the  
8 slippery slopes. So I at least want to make sure we are --

9           **THE COURT:** Sure, exactly.

10          **MR. SAMUELS:** -- all aware of what the fees are.

11          **THE COURT:** Uh-huh.

12          **MR. SAMUELS:** So that's 1.5 percent of \$25 million,  
13 which is \$375,000, as I understand it. Then the unused  
14 facility fee is on the unused portion of the maximum committed  
15 amount and that's 50 basis points. So that's if they didn't  
16 use it at all, that would be another \$125,000, as I understand  
17 it. Then there is the collateral management fee of 10,000 per  
18 quarter and there is the due diligence fee. So your Honor's  
19 reference to 2 and a half million dollars of commitment fees, I  
20 wasn't quite sure where that number had come from. That's not  
21 the correct number.

22          **THE COURT:** No, the point was that there's two  
23 million -- well, yeah. You're only lending -- the commitment  
24 fee is one half --

25          **MR. SAMUELS:** I don't think you could --

1           **THE COURT:** -- is 2 percent --

2           **MR. SAMUELS:** I don't think you could add up all the  
3 fees.

4           **THE COURT:** -- 2 percent on 25 million.

5           **MR. SAMUELS:** It's 500,000, Judge.

6           **THE COURT:** Oh, okay, sorry.

7           **MR. SAMUELS:** Okay. Also the reference to LIBOR plus  
8 ten, I think the only place the term sheet even references that  
9 is towards the bottom of Page 4 on the --

10          **THE COURT:** So it costs a half a million plus 10,000  
11 a quarter --

12          **MR. SAMUELS:** It's only half a million if they don't  
13 use the money. If they were to use all of the money, the  
14 unused facility fee would be less.

15          **THE COURT:** No, no, no. The origination fee --

16          **MR. SAMUELS:** One and a half percent, 375,000, yes.

17          **THE COURT:** Okay. Right.

18          **MR. SAMUELS:** Yes.

19          **THE COURT:** Then you've got 50 percent on -- oh,  
20 that's unused. So you've got one and a half percent  
21 nonrefundable origination fee and they're paying interest on  
22 the entire amount.

23          **MR. SAMUELS:** That's correct.

24          **THE COURT:** Okay. So they're paying interest on how  
25 much?

1           **MR. SAMUELS:** They're paying the interest -- well,  
2 they're paying the interest on the -- it depends -- they're  
3 paying interest on the amounts that they draw and they're  
4 paying fees. They're paying a half a percent unused facility  
5 fee on the part that they don't draw.

6           **THE COURT:** So you can anticipate making how much  
7 from this?

8           **MR. SAMUELS:** Well, if they drew all the 25 million  
9 immediately less the fees that would be paid at closing --  
10 let's say they drew \$24 million immediately, LIBOR -- I don't  
11 know what LIBOR -- what one month LIBOR is at right now. Maybe  
12 there's somebody in the room who would know that but LIBOR plus  
13 350 is the rate and I assume that that rate was negotiated at  
14 inception with Mr. Allison. I assume this term sheet is the  
15 product of negotiations that I didn't participate in but I  
16 assume that not only did our client negotiate with Mr. Allison  
17 over this but we were effectively negotiating with others who  
18 were interested in potentially making this DIP loan and they  
19 agreed to our loan -- or our term sheet because it was a more  
20 favorable fee.

21           But in terms of the fees themselves, Judge, there'd  
22 be a 375,000-dollar origination fee. If they used all of the  
23 money, as I understand it, they wouldn't have the unused  
24 facility fee. It's on the unused portion. The collateral  
25 management fee is 10,000 a quarter -- is \$40,000 and then you

1 have the reimbursement of the due diligence costs which we  
2 would hope to keep to the 150,000 but your Honor's reading of  
3 the term sheet is correct.

4 **THE COURT:** Okay. All right.

5 **MR. SAMUELS:** And the last thing I want to say is  
6 your reference to LIBOR plus ten percent, that is only on --

7 **THE COURT:** In the future.

8 **MR. SAMUELS:** -- future fundings if we assess that  
9 it's a particularly risky loan. This was just our best  
10 estimate of what the interest rates on those future loans might  
11 be.

12 **THE COURT:** Now, why in the world will I presume that  
13 you're even going to make this loan since there isn't any  
14 collateral that this Debtor owns other than --

15 **MR. SAMUELS:** Well, that's not true, Judge, because  
16 the loan will be made to all five of the Debtors and the funds  
17 themselves hold mortgages. So, you know, that I -- my  
18 understanding is that the underwriting on this is primarily on  
19 loans that are -- on mortgage loans that are already held by  
20 the funds.

21 **THE COURT:** So in essence, you're going to take your  
22 collateral on the mortgages held by the funds?

23 **MR. SAMUELS:** Well, we're going to have a lien on  
24 everything that the Debtors have, which is standard.

25 **THE COURT:** But the question is this and this is,

1 kind of, one of those due diligence. If you really think -- I  
2 mean, I, kind of, wonder you're going to make the loans because  
3 in reality, USA Commercial owns nothing other than the rights  
4 of the servicing agreement.

5 **MR. SAMUELS:** It has the right to future servicing  
6 fees. It has a lot of assets but --

7 **THE COURT:** Okay. Well, right to future servicing  
8 fees, that's it. It doesn't have any mortgages.

9 **MR. SAMUELS:** No, it also has whatever cash it has in  
10 the bank. It has origination fees on any loans it makes in the  
11 future.

12 **THE COURT:** So -- but you're also going to claim that  
13 entitled to a lien on the loans held by the funds?

14 **MR. SAMUELS:** Yes, absolutely. That's the primary --

15 **THE COURT:** Now, why doesn't that create bigger  
16 problems?

17 **MR. SAMUELS:** For our client?

18 **THE COURT:** No, for this estate.

19 **MR. SAMUELS:** Your Honor, we're making the loan  
20 against collateral. That's what the whole due diligence  
21 process is all about, Judge.

22 **THE COURT:** But what makes you think -- I guess  
23 you're saying that the funds have the right --

24 **MR. SAMUELS:** The funds are themselves direct  
25 investors --

1           **THE COURT:** Right.

2           **MR. SAMUELS:** -- with respect --

3           **THE COURT:** So they have a few loans?

4           **MR. SAMUELS:** They have more than a few loans. They  
5 have a few loans where they are the only direct investors.

6           **THE COURT:** So this loan then would just be against  
7 the collateral of the funds?

8           **MR. SAMUELS:** It would be against all property of the  
9 estate of all five of the Debtors.

10          **THE COURT:** But it would primarily impact the funds?

11          **MR. SAMUELS:** Well, no, I won't say that because  
12 there may be causes of action that the Debtors may have against  
13 third parties.

14          **THE COURT:** And so you're going to take a security  
15 interest in that as well?

16          **MR. SAMUELS:** Absolutely.

17          **THE COURT:** Okay, all right.

18          **MR. SAMUELS:** Absolutely.

19          **THE COURT:** Okay, opposition?

20          **MR. MEROLA:** I just briefly want to go over timing,  
21 your Honor. At the May 3rd hearing where Debtor's Counsel  
22 indicated they wanted to get this commitment fee approved, your  
23 Honor admonished them as to the timing in order to have a  
24 hearing on the 18th. The motion was not filed until the 8th.  
25 There was no term sheet with the motion. On the 10th, my



1 office requested in writing that term sheet. No term sheet was  
2 made available, notwithstanding the fact the hearing was on the  
3 18th, until the night of the 16th.

4           The committees had their first organizational meeting  
5 today -- yesterday. We agree with you. You don't pay the  
6 commitment fee unless you're going to make the loan. No one  
7 has had the time to evaluate whether this is a good, bad or  
8 indifferent loan. The comments your Honor is making from the  
9 bench lead us to indicate that it may not be the best  
10 commercial deal for the estates but at a minimum, the payment  
11 of this commitment fee should be combined with the request to  
12 approve the loan transaction in whole so it can be evaluated so  
13 we avoid the whole camels, nose and the tent problem that we  
14 have here.

15           **THE COURT:** Okay. Any other comments?

16           **MS. DAVIS:** Mr. Merola basically summarized what I  
17 had in my written opposition. So I certainly agree, your  
18 Honor, and I think that we need to look at the whole thing at  
19 the same time and not get everything one day before the hearing  
20 plus an errata at 5:00 o'clock yesterday afternoon to sit down  
21 and try and figure out which loan commitment we're really  
22 talking about.

23           **MR. MEROLA:** And the one thing the errata indicates  
24 is that Mr. Samuels' client is very flexible about when the  
25 drop-dead date is because the only change between the two

1 erratas was the absolute last date that this fee had to be  
2 paid.

3 **THE COURT:** Okay. Oh, let -- Mr. Landis had a  
4 comment first, I think, or else he was just tired of sitting  
5 down. So --

6 **MR. LANDIS:** A little of both of those, your Honor.  
7 I didn't bring the Code this time. I just brought the --

8 **THE COURT:** Okay.

9 **MR. LANDIS:** -- front of my file though because I  
10 wanted to inject a pragmatic aspect into your consideration  
11 too. If my notes are right, we're talking about fees here in  
12 connection with this potential transaction that could total  
13 about \$565,000. We've already paid E&O fees of half a million.  
14 Ray Quinney & Nebeker has a 210,000-dollar retainer, some of  
15 which has already been applied and now we're talking 75,000 to  
16 Schwartzer & McPherson and just doing some quick math, we're  
17 talking about a million four going out of these Debtor estates  
18 in just fees with no money going back to the investors.

19 And the other thing we're talking now is impairing  
20 the mortgages that are held in the funds for the benefit of USA  
21 Commercial Mortgage. Your Honor, I think that with respect to  
22 these fees, I would join simply in the prior comments that were  
23 made with respect to if we're going to do this, let's do it as  
24 an entire motion. Let's set it for another date. That's the  
25 position of our office. Thank you.

1           **THE COURT:** Okay.

2           **MR. SAMUELS:** I just want to correct two things. The  
3 errata was at the Debtor's request because they wouldn't have  
4 had the time to wire-transfer the fee by the 18th. They asked  
5 us to agree to the 19th to reflect the time of day and when the  
6 wire cut off. So that's the only reason for that. That was  
7 the flexibility that we showed there.

8           The other thing is this assumption that people seem  
9 to have that we can do it all as part of the same process and  
10 pay the due diligence fee at the back end. The due diligence  
11 isn't going to happen unless it's paid on the front end. This  
12 assumption that the due diligence has already been done is not  
13 accurate. The client has done real property due diligence on  
14 certain of the properties but not all of the properties. The  
15 lawyers -- our firm has not done any legal due diligence,  
16 hasn't done any drafting of any DIP orders, DIP agreements, any  
17 of that and that -- we are not going to be authorized to do  
18 that at Fortress' risk. That's not the way Fortress does  
19 business. That's not the way the term sheet was negotiated.

20           So this notion that we'll be there whenever you set a  
21 hearing and you can just do it all at the back end, I'm here to  
22 tell you that's not the way it works, Judge. That's why this  
23 was negotiated for an upfront fee so that Fortress wouldn't be  
24 taking the risk of bearing all of the expense including legal  
25 expense and then at the back end find out that your Honor

1 doesn't approve the DIP loan. That's why it's structured this  
2 way and nobody should have any allusions that we can just wrap  
3 it all together in a nice, pretty bow and put it on for hearing  
4 in July. We won't get to July.

5           **THE COURT:** Okay. Well, notwithstanding that, I'm  
6 not going to approve the due diligence fee. I appreciate the  
7 fact that this may mean that Force is not going to make a loan.  
8 I fully understand that but these are the problems I see.  
9 First of all, this Debtor can't afford to spend a hundred and  
10 fifty thousand dollars now and then also face the risk of an  
11 even higher fee because once you've committed to allow in the  
12 doing due diligence, my heavens, due diligence in a case like  
13 this could require the same amount of fees that the Trustee is  
14 spending, hundreds of thousands of dollars.

15           And I'm not so sure that I would say it'd be  
16 unreasonable for them to figure out what loans to make without  
17 having done an analysis of what the fund has and doesn't have  
18 which means they would spend hours on the whole issue of which  
19 is going to be the ultimate question in this case. Is it  
20 property of the estate or isn't it property of the estate?  
21 Secondly, you told me at the last hearing that the Debtor had  
22 sufficient funds to process this at least for 90 days. So we  
23 shouldn't have to borrow monies to do this.

24           To the extent that we may need funds in the future,  
25 then that's something that the -- you know, Mr. Allison can

1 certainly bring forward. Perhaps you'll find a lender.  
2 Perhaps we won't find a lender. I'm just willing to say "No."  
3 I am tired of these companies saying we're not going to do due  
4 diligence unless you pay us up front. Fine. If you think it's  
5 a good deal, then you do it or you don't do it but there's not  
6 any sense in paying the money up front. Nobody else makes that  
7 risk in the real world. So I don't know why Force should  
8 either, especially in light of the fact they're extracting  
9 significant interest and other fees.

10 Now, it may well be -- I mean, and the next thing  
11 perhaps even more important is quite frankly, I doubt they'd  
12 make the loan. How in the world do you make a loan of \$25  
13 million in the collateral we have or don't have in this case?  
14 And then finally, as I said, I'm -- even if they did -- we'll  
15 have to address this at the final hearing but I'd be very  
16 concerned about granting them a lien in that thing because  
17 again as I said, that puts them in a direct conflict with all  
18 these other people about whose loan it is.

19 It may well be this case goes away in the sense that  
20 all that's left is the investors fighting inter se. The Debtor  
21 may be long gone. You know, somebody will be out there  
22 collecting money but the big fight in this case is going to be  
23 who gets the money. As you said, hopefully that's not the  
24 case. Hopefully this money will start coming in but I just  
25 don't see it.

1           So I'm not going to allow the due diligence fee. I'm  
2 quite frankly aware that may, you know, end Mr. Allison's hopes  
3 for getting a loan but I think it just -- the estate just can't  
4 stand the expenditure of that much money at this time. If you  
5 want to bring the loan on its -- you know, if they're willing  
6 to waive that or whatever, that's certainly fine and I  
7 understand Force may go away but that's where I think that  
8 issue has to lie.

9           **MS. JARVIS:** Your Honor, I just wanted to correct one  
10 -- I think one maybe misunderstanding with respect to whether  
11 there is -- there are assets in Commercial Mortgage. You do  
12 recall that we talked this morning about we do have a 58  
13 million-dollar receivable due from IP that we are in the  
14 process of hopefully securing.

15           **THE COURT:** Well, as somebody pointed out in the  
16 oppositions concerning conflicts, query -- why should  
17 Commercial get that collateral as opposed to the fund or some  
18 individual lenders? That's not an easy answer and if we want  
19 Sidley and Austin to do that research, let's get Sidley and  
20 Austin to be Debtor's Counsel then.

21           **MS. JARVIS:** I just mentioned that there is that  
22 asset as well and that, you know, frankly in -- hopefully in  
23 securing this, one of the issues that have been raised is we  
24 would insist on the cost of funds interest rate, meaning the  
25 same that we would have to pay for getting a third party to,

1 you know, come in and finance this while we're collecting that  
2 debt.

3 **THE COURT:** Sure. And again, I just urge the  
4 question, you know, whether it would pencil out. So -- now,  
5 just looking forward to the next hearing, one thing -- I'm  
6 sorry. Do you have a comment, Mr. Merola?

7 **MR. MEROLA:** I just have housekeeping matters for  
8 you.

9 **THE COURT:** Yeah, sure. Well, let me finish my  
10 housekeeping first and then we'll do yours. On the June 5th  
11 hearings, Eileen -- well, we've got the big issue is the motion  
12 to hold funds. I would hope by that time Mr. Allison would be  
13 able to have spreadsheets that show where we are with respect  
14 to each loan because quite frankly, I think people may be  
15 taking positions in this case but they don't know they're going  
16 their own ox and it's not until you see where your particular  
17 loan is that all of a sudden your position changes. Is that  
18 going to be possible to get us a fairly good spreadsheet on an  
19 update of what you did the last time,  
20 Mr. Allison?

21 **MR. ALLISON:** Yes, your Honor.

22 **THE COURT:** Thank you. If you could, if you could  
23 please file that by -- can I ask May 30th? Is that too early?  
24 The reason I wanted to do that was because that way, you know,  
25 people's opposition is going to be due five days before but

1 once they see that, this will give them the opportunity to  
2 withdraw their opposition, to modify it and I would allow  
3 withdrawals or modifications based upon the data you now see.  
4 Can we get that done by May 30th or at least as many loans as  
5 possible?

6 **MR. ALLISON:** Yes, your Honor.

7 **THE COURT:** Okay. So as many loans as possible. I  
8 think that'll really help in seeing where all these various  
9 positions are. Let us also set Mr. -- the committees' motions  
10 to employ --

11 **MR. MEROLA:** Just--

12 **THE COURT:** -- and at that time, we could address the  
13 issue about what committees -- yeah.

14 **MR. MEROLA:** -- real quickly, your Honor, Frank  
15 Merola on behalf of the investor committees. We filed the  
16 applications this morning for both our firm and the Shea &  
17 Carlyon firm. We've requested an order shortening time to the  
18 5th. The U.S. Trustee and the Debtor has consented.

19 **THE COURT:** So I'll agree. That can be set for the  
20 5th as well.

21 **MR. MEROLA:** Your Honor, just briefly because  
22 Mr. Garman did not have the benefit of seeing our application  
23 for commenting on it. Our application provides that we will be  
24 representing the investor committees solely on issues that they  
25 have common interest. It expressly acknowledged the



1 possibility that conflicts might exist between the investor  
2 committees and that conflict Counsel will be in place to handle  
3 those conflicts.

4           This was an organic thing, your Honor. We were  
5 contacted by more than one of the committees. The committees  
6 spoke amongst themselves and decided that the key to this case  
7 was coordinating the efforts of the investor committees and it  
8 was concluded that the best way to coordinate those efforts was  
9 through a single law firm on issues of common interest. We've  
10 gone up and down. You'll see the protocols we have for the  
11 conflict issue. It's not something we take lightly and we're  
12 prepared to address it.

13           **THE COURT:** Well, and again, you know, it's -- and I  
14 -- it goes back to my comments to the U.S. Trustee before. In  
15 the perfect world, there would be Counsel for every kind of  
16 interest but that means that all the money would go to the  
17 professionals and that -- you know, professionals may say,  
18 yeah, that's the perfect world and none go to the --

19           **MR. MEROLA:** Your Honor, after sitting with my  
20 partner Mr. Davidson for more hours than I want to admit, I  
21 concluded that the only solution to eliminate all the conflicts  
22 in this case would be to have 115 lawyers for each of the loans  
23 but once you start talking about entities, once you start  
24 talking about even individual investors, they're all over the  
25 map and you've got to be pragmatic at some point.

1           The other issue I have, your Honor, is now that we  
2 have official committees appointed, we will be requesting  
3 hopefully here on the record and if we have to in writing and  
4 hopefully not through a motion that attorneys that appear on  
5 behalf of groups of investors or more than one party comply  
6 with Rule 2019 so we know who's out there. A lot of these  
7 alliances are changing. We have attorneys here today that are  
8 making appearances on different groups of investors that they  
9 made appearances on previously and if we're going to be -- just  
10 in order to keep some order in this -- if you're going to be  
11 throwing rocks, we have to know whose rocks they're throwing.

12           **THE COURT:** Yeah, and, you know, we probably should  
13 have included that in the case administration order. I know I  
14 mentioned that at the last hearing. I didn't think to catch it  
15 but let me make it clear that everybody -- I mean, it's in the  
16 Rules already but anybody who represents more than one entity  
17 -- tell me again the name of that rule so -- the number of that  
18 rule so we can just read it.

19           **MS. JARVIS:** It's 2019.

20           **MR. UNIDENTIFIED:** 2019.

21           **THE COURT:** 2019.

22           **MS. JARVIS:** And your Honor, we had raised that too.  
23 It's a difficulty for us in responding when we can't figure --  
24 they just, kind of, say we --

25           **THE COURT:** Right.

1           **MS. JARVIS:** -- represent a bunch of people and we  
2 don't know who they are.

3           **THE COURT:** Okay. So let me just remind the  
4 attorneys here that under 2019 in a Chapter 11 except with  
5 respect to a committee, every entity or committee representing  
6 more than one creditor or equity security holder shall file a  
7 verified statement setting forth the name and address of the  
8 creditor or equity security holder, nature and amount of the  
9 claim or interest and the time of acquisition unless it's more  
10 than one year prior to the filing, a recital of the pertinent  
11 facts and circumstances in connection with the employment and  
12 in the name of the committee, the names of the entities  
13 directly or indirectly who arranged the employment and the time  
14 of employment. And I'm just paraphrasing. Obviously the rule  
15 is what you've got to read.

16           **MS. DAVIS:** Your Honor, if I might be heard briefly?

17           **THE COURT:** Uh-huh.

18           **MS. DAVIS:** My clients are direct lenders. We're not  
19 creditors. We're not equity holders. I'm happy to comply with  
20 the Court's requirement but they're parties of interest and  
21 they have claims to get their own property out of this estate.

22           **THE COURT:** Let me modify and say that I'm going to  
23 make it apply to anybody who represents a creditor, equity  
24 security holder or a direct lender and the point being, this is  
25 more of a way to keep track of who represents who. If nothing

1 else, it will help everybody to talk beforehand and know what  
2 kind of interest they have and if you represent somebody who  
3 has more capacities, that will help us understand, you know, in  
4 what place their talking.

5 I might mention to all the Counsel out here who  
6 represent several different entities and those entities may  
7 have -- like, let's say one entity has -- is a direct lender  
8 and is also a member of the LLC and the other entity it  
9 represents is only a direct lender, you may have to advise your  
10 two clients as to potential conflicts there as well. Again,  
11 they're only potential but everybody's got the same problem in  
12 this case and I'm not suggesting that everybody get different  
13 Counsel but, boy, you've got to be aware of that.

14 Again, I think we'll know more certainly at the next  
15 hearing. Certainly we'll know -- the July 27th hearing is  
16 going to be very important. We'll know a lot more by then.  
17 Yeah, go ahead.

18 **MR. MEROLA:** Your Honor, just to be clear, the OSTs  
19 for both our firm and the Shea & Carlyon firm for the hearing  
20 on the 5th are approved.

21 **THE COURT:** Yes.

22 **MR. MEROLA:** Ms. Carlyon has corrected me. Her  
23 application has not been on file but will be contemporaneously.

24 **THE COURT:** That's fine. That's fine. Does anybody  
25 anticipate filing in the next -- I'm sorry. Let me go back.

1 What else do we have set for the 5th right now? Does anybody  
2 know off the top of their head?

3 **MS. JARVIS:** The Hilco retention application.

4 **THE COURT:** Okay. The Hilco.

5 **MS. DAVIS:** I believe Mr. LePome filed some motions  
6 as well.

7 **THE COURT:** Okay.

8 **MS. CARLYON:** There are a number of motions --

9 **THE COURT:** Oh, Ms. Chubb.

10 **MR. UNIDENTIFIED:** And Ms. Chubb.

11 **MS. CARLYON:** -- filed. Ms. Chubb filed motions to  
12 not pay the appraiser. There are motions to not hold money.  
13 There are motions to pay money. There are other issues related  
14 to this.

15 **THE COURT:** Okay, okay.

16 **MR. MEROLA:** Countermotions.

17 **THE COURT:** Exactly, in essence. As I indicated  
18 before, that I was -- I wanted countermotions filed rather than  
19 just oppositions just because it's going to make things  
20 clearer. Let me remind all of you again that in your captions  
21 if the reply -- indicate what Debtors it applies to. Just as a  
22 little technical thing, it's a lot easier and I know that the  
23 name of the cases are hard -- if you could put the caption,  
24 somehow work it in. If you could put the title of your case on  
25 the front page so that I know what it is, so the title of the

1 caption and what it is, just so that I can see what it is  
2 easier. It's no big deal. It just, you know, helps get  
3 through this stuff a lot quicker.

4 Eileen, we need -- let's set aside the whole day of  
5 the 5th. We're going to have to move -- do something about  
6 that trial date.

7 **THE CLERK:** Okay.

8 **THE COURT:** So we'll give you all day the 5th and  
9 we'll take a recess at noon rather than going straight through,  
10 just to assist in your planning because I am sure that hearing  
11 will just take a long, long time. I think that's it.

12 **MR. SCHWARTZER:** Your Honor, with regard to the case  
13 management order, do you want me to prepare a supplemental case  
14 management order that refers to the sanctions and to the fact  
15 that 2019 will apply to everybody?

16 **THE COURT:** Yes, let's do that. Okay. Just call it  
17 a supplemental.

18 **MR. SCHWARTZER:** Okay.

19 **THE COURT:** It adopts all the prior provisions and  
20 just supplements. Okay, great. All right, thank you very  
21 much.

22 **THE CLERK:** All rise.

23 **(This proceeding was adjourned at 1:11 p.m.)**  
24  
25

CERTIFICATION

I certify that the foregoing is a correct transcript from the electronic sound recording of the proceedings in the above-entitled matter.

A handwritten signature in cursive script, appearing to read "Toni Hudson", is positioned above a horizontal line.

Signed

July 9, 2010

Dated

*TONI HUDSON, TRANSCRIBER*